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CIS

SOCIAL SECURITY RETIREMENT TEST

HEARING

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

SEPTEMBER 29, 1988

Serial 100-91

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SOCIAL SECURITY RETIREMENT TEST

THURSDAY, SEPTEMBER 29, 1988

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON SOCIAL SECURITY,
Washington, DC.

The subcommittee met, pursuant to call, at 10:30 a.m., in room B-318, Rayburn House Office Building, Hon. Andy Jacobs, Jr. (chairman of the subcommittee) presiding.

[The press release announcing the hearing and profiles of introduced bills on the subject of the hearing follow:]

FOR IMMEDIATE RELEASE
WEDNESDAY, SEPTEMBER 14, 1988

SUBCOMMITTEE ON SOCIAL SECURITY #13
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
1102 LONGWORTH HOUSE OFFICE BLDG.
WASHINGTON, D.C. 20515
TELEPHONE: (202) 225-1721

ANDY JACOBS, JR. (D., IND.),
CHAIRMAN, SUBCOMMITTEE ON SOCIAL SECURITY,
COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES,
ANNOUNCES A HEARING ON THE SOCIAL SECURITY RETIREMENT TEST,
ON THURSDAY, SEPTEMBER 29, 1988, AT 10:30 A.M.,
IN ROOM B-318 RAYBURN HOUSE OFFICE BUILDING

Andy Jacobs, Jr. (D., Ind.), Chairman of the Subcommittee on Social Security, Committee on Ways and Means, U.S. House of Representatives, announced today that the Subcommittee will hold a hearing on the social security retirement test. The hearing will be held on Thursday, September 29, 1988, in room B-318 Rayburn House Office Building, beginning at 10:30 a.m.

The social security retirement test reduces or eliminates benefits for individuals who earn income above certain annually-adjusted limits. Currently, individuals under age 65 may earn up to $6,120 a year in wages or self-employment income without their benefits being affected. Persons aged 65-69 may earn up to $8,400 a year. The exempt amounts are adjusted each year to reflect changes in average wages in the economy. For earnings in excess of these amounts, $1 of benefits is lost for each $2 of earnings. Beginning in 1990, beneficiaries aged 65-69 will lose only $1 in benefits for every $3 in earnings in excess of the limit. Persons aged 70 years and older are not subject to the test.

Several proposals have been made to eliminate the retirement test or to raise the limitation. These include both proposals made by Members of Congress, and a proposal made by the Social Security Administration and the Department of Health and Human Services (HHS) to the President in late 1987. Under the HHS proposal, the retirement test would have been phased out for those 65 and over during a five-year period. The President has not made a recommendation to the Congress.

The Congressional Budget Office (CBO) has recently completed a study for the Subcommittee of the distributional impact of eliminating the retirement test or raising the limitation. The study shows which workers are affected by the current retirement test - by income, sex and living arrangement - and it shows which individuals would benefit from an increase in, or elimination of, the limitation.

The Subcommittee will receive testimony from CBO describing its main findings. In addition, the Subcommittee will receive testimony from the Social Security Administration as well as from Members of Congress and public witnesses who wish to testify.

DETAILS FOR SUBMISSION OF REQUESTS TO BE HEARD:

Requests to be heard at the hearing must be made by telephone to Harriett Lawler or Diane Kirkland [(telephone 225-1721)] by close of business Thursday, September 22, 1988. In order to facilitate scheduling, requests should indicate the specific issues that the witness wishes to address and the relative priority of each issue if more than one issue is indicated. The request should be followed by a formal written request addressed to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, room 1102 Longworth House Office Building, Washington, D.C. 20515. The Subcommittee will notify by telephone those scheduled to appear

(MORE)

as soon as possible after the filing deadline. Any questions concerning a scheduled appearance should be directed to the Subcommittee staff [(202) 225-9263)].

In view of the limited time available to hear witnesses, the Subcommittee may not be able to accommodate all requests to be heard. Those persons and organizations not scheduled for an oral appearance are encouraged to submit written statements for the record of the hearing. All persons requesting to be heard, whether they are scheduled for oral testimony or not, will be notified as soon as possible after the filing deadline.

Witnesses scheduled to present oral testimony are required to summarize briefly their written statements in no more than five minutes. THE FIVE-MINUTE RULE WILL BE STRICTLY APPLIED. The full statement will be included in the printed record.

In order to assure the most productive use of the limited amount of time available to question witnesses, those scheduled to appear before the Subcommittee are required to submit 100 copies of their prepared statements to the Subcommittee on Social Security office, room B-316 Rayburn House Office Building, at least 24 hours in advance of their scheduled appearances. Failure to do so may result in the witness being denied the opportunity to testify in person.

WRITTEN STATEMENTS IN LIEU OF PERSONAL APPEARANCE:

Persons submitting written statements for the printed record of the hearing should submit six (6) copies by the close of business, Thursday, October 13, 1988, to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, room 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing a written statement for the record of the printed hearing wish to have their statements distributed to the press and the interested public at the hearing, they may provide 75 additional copies for this purpose to the Subcommittee office, room B-316 Rayburn House Office Building, during the course of the public hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be typed in single space on legal-size paper and may not exceed a total of 10 pages.
2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.
3. Statements must contain the name and capacity in which the witness will appear or, for written comments, the name and capacity of the person submitting the statement, as well as any clients or persons, or any organization for whom the witness appears or for whom the statement is submitted.
4. A supplemental sheet must accompany each statement listing the name, full address, a telephone number where the witness or the designated representative may be reached and a topical outline or summary of the comments and recommendations in the full statement. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press and public during the course of a public hearing, may be submitted in other forms.

********** 100TH CONG. STATUS PROFILE FOR H.R.42 **********
SPONSOR..... Archer
DATE INTRODUCED... January 6, 1987
HOUSE COMMITTEE... Ways and Means
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act so as to remove the limitation upon the amount of outside income which an individual may earn while receiving benefits thereunder.
RELATED BILLS -- House Designation
H.R.365 (Identical), H.R.248 (Identical).
CO-SPONSORS..... 21 CURRENT COSPONSORS --
Jan 6, 87 Referred to House Committee on Ways and Means.
Jan 13, 87 Referred to Subcommittee on Social Security.
COS CO-SPONSORS..... 21 CURRENT COSPONSORS --
Feb 4, 87 Broomfield.
Mar 11, 87 Daub, Armey.
Apr 6, 87 Vucanovich.
Oct 7, 87 Stump, Walker, Frank, Lagomarsino, Badham, Donald Lukens, Bilirakis, Saxton, Porter, DeFazio, Oxley, Collins, Frost, Roe.
Jan 25, 88 Applegate.
Feb 8, 88 Buechner.
Mar 1, 88 Fields.
BD BILL DIGEST ..... Jan 6, 87. Amends title II (Old Age, Survivors and Disability Insurance) of the Social Security Act to remove the limitation on the amount of outside income which a beneficiary may earn without incurring a reduction in benefits.

********** 100TH CONG. STATUS PROFILE FOR H.R.620 **********
BRIEF TITLE..... Elderly Earnings Opportunity Act of 1987
SPONSOR..... Wyden
DATE INTRODUCED... January 20, 1987
HOUSE COMMITTEE... Ways and Means
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act to ease the burden currently imposed by excessive earnings test requirements.
CO-SPONSORS..... 1 CURRENT COSPONSOR --
Jan 20, 87 Referred to House Committee on Ways and Means.
Jan 27, 87 Referred to Subcommittee on Social Security.
COS CO-SPONSORS..... 1 CURRENT COSPONSOR --
Jan 25, 88 Boucher.
BD BILL DIGEST ..... Jan 20, 87. Elderly Earnings Opportunity Act of 1987 - Amends title II (Old Age, Survivors and Disability Insurance) of the Social Security Act to make uniform for all beneficiaries: (1) the amount of outside income which beneficiaries may earn without incurring a reduction in benefits; and (2) the percentage of nonexempt earnings which are deducted from benefits as excess earnings. Adds $1,000, until the year 2000, to the annual outside income which a beneficiary may earn without incurring a benefit reduction.

Directs the Secretary of Health and Human Services to conduct an ongoing study to determine whether further modifications of the treatment of a beneficiary's outside income are necessary or appropriate. Sets forth reporting requirements.

********** 100TH CONG. STATUS PROFILE FOR H.R.1204 **********

BRIEF TITLE..... Social Security Earnings Test Limitation Act of 1987
SPONSOR..... Brown (CO)
DATE INTRODUCED... February 24, 1987
HOUSE COMMITTEE... Ways and Means
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act to eliminate the earnings test for individuals who have attained retirement age.
CO-SPONSORS..... 2 CURRENT COSPONSORS --
Feb 24, 87 Referred to House Committee on Ways and Means.
Mar 3, 87 Referred to Subcommittee on Social Security.

COS CO-SPONSORS..... 2 CURRENT COSPONSORS --
Mar 2, 88 Fields.
May 3, 88 Hefley.

BD BILL DIGEST ..... Feb 24, 87. Social Security Earnings Test Limitation Act of 1987 - Amends title II (Old Age, Survivors and Disability Insurance) of the Social Security Act to remove the limitation on the amount of outside income which beneficiaries who have attained retirement age may earn without incurring a reduction in benefits.

********** 100TH CONG. STATUS PROFILE FOR H.R.1555 **********

SPONSOR..... Daub
DATE INTRODUCED... March 11, 1987
HOUSE COMMITTEE... Ways and Means
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act to phase out the earnings test over a 4-year period for individuals who have attained age 65.
CO-SPONSORS..... 3 CURRENT COSPONSORS --
Mar 11, 87 Referred to House Committee on Ways and Means.
Mar 17, 87 Referred to Subcommittee on Social Security.

COS CO-SPONSORS..... 3 CURRENT COSPONSORS --
Dec 11, 87 Jeffords.
Jan 25, 88 Emerson.
Aug 4, 88 McEwen.

BD BILL DIGEST ..... Mar 11, 87. Amends title II (Old Age, Survivors and Disability Insurance) of the Social Security Act to increase for each year from 1988 through 1991 the amount of outside income which beneficiaries who have attained retirement age may earn without incurring a reduction in benefits. Removes such income limitation thereafter.

********** 100TH CONG. STATUS PROFILE FOR H.R.3794 **********

BRIEF TITLE..... Worker's Option Act of 1988
SPONSOR..... Archer
DATE INTRODUCED... December 18, 1987
HOUSE COMMITTEE... Ways and Means
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act to phase out the retirement earnings test at ages above retirement age, to increase accordingly the delayed retirement credit rate, to exclude accordingly certain earnings in post-retirement years from benefit computations, to prohibit retroactive entitlement to reduced benefits before retirement age, and to authorize for five years appropriations of resulting revenue increases to the Federal Old-Age and Survivors Insurance Trust Fund.

CO-SPONSORS..... 36 CURRENT COSPONSORS --
Dec 18, 87 Referred to House Committee on Ways and Means.
Jan 4, 88 Referred to Subcommittee on Social Security.

COS CO-SPONSORS..... 36 CURRENT COSPONSORS --
Jan 25, 88 Crane, Applegate
Feb 8, 88 Duncan.
Mar 1, 88 Ritter, Davis (IL), Miller (WA), Brown (CO), Lagomarsino, Bunning, Fields, Shumway, Wortley, Armey.
Mar 31, 88 McGrath, Bartlett, Robert Smith (NH), Coats, Roberts, Ballenger, Inhofe, Marlenee, Craig, Goodling, Fish.
Apr 20, 88 Buechner, Combest, Chandler.
Apr 29, 88 Meyers (KS), Hefley.
May 12, 88 Hutto, Shaw.
May 24, 88 Gilman, Broomfield.
Aug 11, 88 Cheney, Smith (TX), Grandy.

BD BILL DIGEST ..... Dec 18, 87. Worker's Option Act of 1988 - Amends title II (Old Age, Survivors and Disability Insurance) (OASDI) of the Social Security Act to phase out, by 1993, the limitation on the amount of outside income which beneficiaries who have attained retirement age may earn without incurring a reduction in benefits. Increases the delayed retirement credit rate for individuals who work beyond retirement age. Phases out the recomputation of an individual's primary insurance amount when such individual has wages or self-employment income after entitlement to old-age or disability insurance benefits. Charges off an individual's excess earnings by eliminating such individual's entitlement to retroactive OASDI benefits for months preceding such individual's attainment of retirement age. Authorizes the appropriation of revenues received by reason of this Act's amendments to the Federal Old-Age and Survivors Insurance Trust Fund from 1989 through 1993.

********** 100TH CONG. STATUS PROFILE FOR S.1777 **********

SPONSOR..... Armstrong
DATE INTRODUCED... October 8, 1987
SENATE COMMITTEE.. Finance
OFFICIAL TITLE.... A bill to amend title II of the Social Security Act to phase out the earnings test over a 5-year period for individuals who have attained retirement age, and for other purposes.
CO-SPONSORS..... 11 CURRENT COSPONSORS --
Oct 8, 87 Referred to Senate Committee on Finance.

COS CO-SPONSORS..... 11 CURRENT COSPONSORS --
Oct 28, 87 Symms, Hecht, Kasten.
Oct 30, 87 Durenberger.
Nov 20, 87 Wilson (CA), Lugar.
Mar 15, 88 D'Amato.
Mar 21, 88 Grassley.
Aug 4, 88 Karnes.
Aug 5, 88 Helms.
Sep 14, 88 Exon.

BD BILL DIGEST ..... Oct 8, 87. Amends title II (Old Age, Survivors and Disability Insurance) of the Social Security Act to increase by $3,000 for each year from 1990 through 1994 the amount of outside income which beneficiaries who have attained retirement age may earn without incurring a reduction in benefits. Removes such income limitation thereafter. Accelerates the effective dates of increases in the delayed retirement credit rate for individuals who work beyond retirement age.

Chairman JACOBS. This will convene the hearing by the Ways and Means Social Security Subcommittee.

The question today is whether under the social security system retirement benefits should be paid to people who are not retired. Ms. Gordon is our first witness from CBO, and you are most welcome, as always.

STATEMENT OF NANCY M. GORDON, ASSISTANT DIRECTOR FOR HUMAN RESOURCES AND COMMUNITY DEVELOPMENT, CONGRESSIONAL BUDGET OFFICE, ACCOMPANIED BY BOB WILLIAMS AND PAUL CULLINAN

Ms. GORDON. Thank you very much, Mr. Chairman.

I am pleased to appear before the subcommittee to discuss CBO's most recent report. With me are Bob Williams, the paper's principal author, and Paul Cullinan, who is responsible for CBO cost estimates for Social Security.

Today I would like to summarize briefly how the earnings test works and the results of our study. I would appreciate my prepared statement being included in the record.

Chairman JACOBS. It is unusual, but we will do it.

Ms. GORDON. Thank you very much.

The Social Security earnings test reduces payments to beneficiaries under age 70 whose earnings exceed specified limits. In 1988, beneficiaries aged 65 through 69 can earn up to $8,400 without having payments withheld, while beneficiaries under age 65 face a lower earnings limit of $6,120. For each $2 of earnings that exceed the limit, Social security benefits are reduced by $1. Beneficiaries are no longer subject to the earnings test once they reach age 70.

Two additional factors affect the operation of the earnings test. First, people who begin receiving benefits during the year are subject to a monthly earnings test: benefits are withheld if monthly earnings exceed one-twelfth of the annual earnings limit. Second, people whose benefits are partially or completely withheld during a month are compensated through a delayed retirement credit [DRC], which increases future benefits by 0.25 percent for each month benefits are reduced—or 3 percent per year. While the DRC at its current level does not fully compensate those whose benefits are completely withheld, it is scheduled to rise to eight percent per year for beneficiaries turning 62 in 2005 or later, at which time it is projected to be actuarially fair.

The earnings test directly affects only a small fraction of the eight million people aged 65 through 69 who are eligible to receive Social Security. As figure 1 shows, 81 percent of people in that group did not work at all in 1986, and another 12 percent had earnings below the earnings limit. Thus, only about 7 percent—or about 600,000 people—either had benefits partially or fully withheld, or elected not to apply for benefits, because of the earnings test. It is likely, however, that somewhat more than this 7 percent were affected by the earnings test; some beneficiaries may have chosen to work less to hold their earnings below the limit and thereby avoid having benefits withheld.

Turning now to the bottom of page four of the prepared statement, many arguments are made about modifying the earnings

test. People who propose to raise the earnings limit or eliminate the test base their position primarily on three arguments. First, they assert that Social Security is a pension for which people have paid and therefore it would be unfair to penalize those who continue to work. Second, they argue that the high implicit tax rates for beneficiaries who work cause older people to work less than they would otherwise choose. Finally, they maintain that the earnings test is complicated and costly to administer.

Proponents of retaining the earnings test base their support on the belief that Social Security is primarily a program to replace lost earnings and thus should not provide payments to those who continue to earn large amounts. Furthermore, they assert, Social Security is not like pension programs: its benefit structure pays relatively more to those with low earnings than to those with high earnings; moreover, it provides rates of return on contributions that are much higher than those paid by private pensions, at least for current retirees.

Based on CBO's analysis, the people who would no longer be affected if the earnings test were eliminated would be among the best off of all beneficiaries. Figure 2 shows that while only 13 percent of all beneficiaries aged 65 through 69 had family income above $42,000 in 1986, over 40 percent of the people who would gain from removing the earnings test would have incomes above that level. In contrast, people with incomes below $15,000 made up nearly 40 percent of all beneficiaries but only about 5 percent of those who would gain from eliminating the earnings test. Finally, about half of all beneficiaries and a similar fraction of those who would benefit from eliminating the earnings test had incomes between $15,000 and $42,000. Of those beneficiaries no longer affected, nearly two-thirds would be men and about 70 percent would be married.

Raising the earnings limit—but not removing the earnings test entirely—would also focus gains on beneficiaries who are best off, but a higher proportion of the gains would go to people with low family incomes. For example, doubling the earnings limit—to just over $17,000 in 1989—would exempt from the earnings test about 45 percent of beneficiaries aged 65 through 69 currently affected by the test; this group would include most of the women, widows and widowers, and people with family incomes below $25,000 who are now affected. At the same time, doubling the limit would leave four-fifths of beneficiaries with family incomes above $42,000 still subject to having benefits withheld, although many of these high-income beneficiaries would gain from the change.

Turning now to the effects on the Federal budget, outlays for Social Security would increase if the earnings test were relaxed or eliminated, but the costs would be much higher for larger changes, as table 1 shows. For example, raising the earnings limit to $10,000 in 1989 would increase outlays by about $1.3 billion over the 1989–1993 period, but doubling it—to $17,280 in 1989—would cost six times as much—more than $8 billion over the 5-year period. Increasing the 1989 earnings limit to $25,000 would raise outlays by nearly $11 billion over the 1989–1993 period, while eliminating it entirely would cost nearly $24 billion over the same 5 years. These

estimates include additional payments to workers who would apply for benefits as a result of the change in earnings test.

Thank you, Mr. Chairman. That concludes my prepared remarks.

[The prepared statement of Nancy M. Gordon, and a CBO study, follow:]

Statement of
Nancy M. Gordon
Assistant Director
for
Human Resources and Community Development
Congressional Budget Office

before the
Subcommittee on Social Security
Committee on Ways and Means
U.S. House of Representatives

September 29, 1988

NOTICE

This statement is not available for public release until it is delivered at 10:30 a.m. (EDT), Thursday, September 29, 1988.

More than 20 bills have been introduced in the 100th Congress to relax or eliminate the Social Security earnings test. In response to a request from this subcommittee, the Congressional Budget Office (CBO) has prepared a staff working paper that discusses the effects of the earnings test on people aged 65 through 69 and examines selected options for changing the test. This statement is based on that study and addresses three topics:

- How the earnings test works;
- The characteristics of people who would no longer be affected by the earnings test if it were eliminated or the earnings limit were raised; and
- The effects on federal outlays of eliminating the earnings test entirely or raising the earnings limit.

HOW THE EARNINGS TEST WORKS

The Social Security earnings test--sometimes called the retirement test--reduces payments to beneficiaries under age 70 whose earnings exceed specified limits. In 1988, beneficiaries aged 65 through 69 can earn up to $8,400 without having payments withheld, while beneficiaries under age 65 face a lower earnings limit of $6,120. For each $2 by which earnings exceed the limit, Social Security benefits are reduced by $1. (In 1990, the reduction will drop to $1 for each $3 of excess earnings for beneficiaries aged 65 through 69; the reduction rate will not change for those under age 65.) Beneficiaries are no longer subject to the earnings test once they reach age 70.

Two additional factors affect the operation of the earnings test. First, people who begin receiving benefits during the year are subject to a monthly earnings test: benefits are withheld if monthly earnings exceed one-twelfth of the annual earnings limit. Second, people whose benefits are partially or completely withheld during a month are compensated through a delayed retirement credit (DRC), which increases future benefits by 0.25 percent for each month benefits are reduced--or 3 percent per year. While the DRC at its current level does not fully compensate those whose benefits are fully withheld, it is scheduled to rise to 8 percent per year for beneficiaries turning 62 in 2005 or later, at which time it is projected to be actuarially fair.

The earnings test directly affects only a small fraction of the 8 million people aged 65 through 69 who are eligible to receive Social Security. As Figure 1 shows, 81 percent of people in that group did not work at all in 1986, and another 12 percent had earnings below the earnings limit. Thus, only about 7 percent--or about 600,000 people--either had benefits partially or fully withheld, or elected not to apply for benefits, because of the earnings test. It is likely, however, that somewhat more than this 7 percent were affected by the earnings test; some beneficiaries may have chosen to work less to hold their earnings below the limit and thereby avoid having benefits withheld.

DATA AND LIMITATIONS OF THE ANALYSIS

CBO's analysis of the characteristics of the people affected by the earnings test is based on data from the Current Population Survey (CPS), the major source of information used to calculate government statistics on unemployment, family incomes, and poverty. These data were chosen because, unlike other sources including the Social Security Administration's administrative records, the CPS reports both annual earnings and total annual family income, as well as information about other characteristics of families.

Data limitations constrain the analysis in three ways, however. First, the CPS does not identify all people aged 65 through 69 who could be receiving Social Security and who therefore could be affected by the earnings test. Consequently, the analysis assumes that all people in that age group with incomes above the earnings limit are eligible for benefits, even if none is reported on the CPS. Second, because data on monthly earnings are not available, the analysis excludes those people who appear to be subject to the monthly earnings test. Finally, and most important, without information on primary insurance amounts, the analysis cannot determine by how much Social Security payments would rise for individual recipients if the earnings test were changed or eliminated. Instead, the analysis is limited to looking at the characteristics of beneficiaries who would be made exempt from having benefits withheld if the earnings limit were raised or the earnings test were removed. These limitations do not apply to estimates of budgetary effects, however, because those estimates are based on other data.

MODIFYING THE EARNINGS TEST

People who propose to raise the earnings limit or eliminate the earnings test entirely base their position primarily on three arguments. First, they assert that Social Security is a pension for which people have paid and therefore it would be unfair to penalize those who continue to work. Second, they argue that the high implicit tax rates for beneficiaries who work cause elder people to work less than they would otherwise choose.1/ Finally, they maintain that the earnings test is complicated and costly to administer.

Proponents of retaining the earnings test base their support on the belief that Social Security is primarily a program to replace lost earnings and thus should not provide payments to those who continue to earn large amounts. Furthermore, they assert, Social Security is not like pension programs: its benefit structure pays

FIGURE 1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 WHO ARE ELIGIBLE FOR SOCIAL SECURITY (By earnings)

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

1. In addition to the $1 reduction in Social Security for each $2 of earnings over the limit, beneficiaries who earn more than $8,400 must pay federal income and payroll taxes, plus state and local taxes. For workers in the lowest federal income tax bracket, the marginal tax rate is therefore more than 72 percent until their benefits are fully withheld.

relatively more to those with low earnings than to those with high earnings; moreover, it provides rates of return on contributions that are much higher than those paid by private pensions, at least for current retirees.

Based on CBO's analysis, the people who would no longer be affected if the earnings test were eliminated would be among the best off of all beneficiaries. Figure 2 shows that while only 13 percent of all beneficiaries aged 65 through 69 had family income above $42,000 in 1986, over 40 percent of the people who would gain from removing the earnings test would have incomes above that level. In contrast, people with incomes below $15,000 made up nearly 40 percent of all beneficiaries but only about 5 percent of those who would gain from eliminating the earnings test. Finally, about half of all beneficiaries and a similar fraction of those who would benefit from eliminating the earnings test had incomes between

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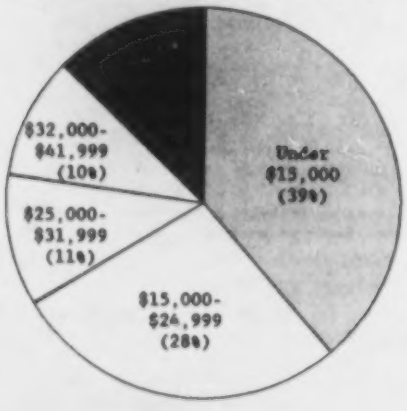
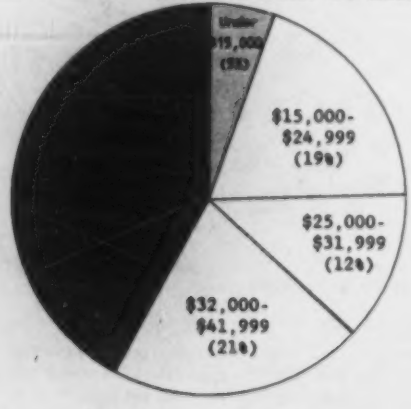
FIGURE 2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 WHO ARE ELIGIBLE FOR SOCIAL SECURITY AND AFFECTED BY THE EARNINGS TEST (By family income)

ALL PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY



PEOPLE WHO WOULD GAIN FROM ELIMINATING THE EARNINGS TEST



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

$15,000 and $42,000. Of those beneficiaries no longer affected, nearly two-thirds would be men and about 70 percent would be married.

Raising the earnings limit--but not removing the earnings test entirely--would also focus gains on beneficiaries who are best off, but a higher proportion of the gains would go to people with low family incomes. For example, doubling the earnings limit--to just over $17,000 in 1989--would exempt from the earnings test about 45 percent of beneficiaries aged 65 through 69 currently affected by the test; this group would include most of the women, widows and widowers, and people with family incomes below $25,000 who are now affected. At the same time, doubling the limit would leave four-fifths of beneficiaries with family incomes above $42,000 still subject to having benefits withheld, although many of these high-income beneficiaries would gain from the change.

EFFECTS ON FEDERAL OUTLAYS

Federal budget outlays for Social Security would increase if the earnings test were relaxed or eliminated, but the costs would be much higher for larger changes, as Table 1 shows. For example, raising the earnings limit to $10,000 in 1989 would increase outlays by about $1.3 billion over the 1989-1993 period, but doubling it (to $17,280 in 1989) would cost six times as much--more than $8 billion over the five-year period. Increasing the 1989 earnings limit to $25,000 would raise outlays by nearly $11 billion over the 1989-1993 period, while eliminating it entirely would cost nearly $24 billion over the same five years. These estimates include additional payments to workers who would apply for benefits as a result of the change in the earnings test.

Because estimating practices used by the Congressional Budget Office are based on a baseline macroeconomic forecast that incorporates projections of aggregate wages and employment, no

TABLE 1. EFFECTS ON OUTLAYS OF OPTIONS FOR CHANGING THE SOCIAL SECURITY EARNINGS TEST FOR PEOPLE AGED 65-69, 1989-1993 (By fiscal year, in billions of dollars)

Option	1989	1990	1991	1992	1993	Total, 1989-1993
Raise 1989 Earnings Limit to $10,000	0.2	0.3	0.3	0.3	0.3	1.3
Double 1989 Earnings Limit to $17,280	1.2	1.7	1.7	1.7	1.8	8.2
Increase 1989 Earnings Limit to $25,000	1.7	2.4	2.3	2.3	2.3	11.0
Eliminate Earnings Test	3.7	5.1	5.0	5.0	5.1	23.9

SOURCE: Congressional Budget Office estimates.

NOTE: Estimates assume that each option would be implemented on January 1, 1989, and that the limit would be indexed according to current law. They also incorporate the effects of additional applications for Social Security benefits.

Details may not add to totals because of rounding.

revenue effects are estimated for the options to change the earnings test. However, when revenue effects have been considered--as they are in the Social Security Administration's estimates--they offset only a small portion (10 percent to 15 percent) of the additional benefit costs.

Finally, the budgetary estimates do not include savings in administrative costs. These costs would, however, be quite small; the Social Security Administration calculates that administrative savings would offset only 1 percent of additional benefit payments. Administrative savings could be significantly larger if the earnings test were eliminated for all age groups.

THE SOCIAL SECURITY EARNINGS TEST AND OPTIONS FOR CHANGE

Staff Working Paper
September 1988

Congress of the United States
Congressional Budget Office

PREFACE

Numerous bills have been introduced in the Congress to raise or eliminate the Social Security earnings test limit for people aged 65 through 69. At the request of the Subcommittee on Social Security of the Committee on Ways and Means, the Congressional Budget Office (CBO) prepared this paper examining who among those aged 65 through 69 are affected by the current earnings test and who would no longer be affected if the earnings test were liberalized or eliminated.

Roberton Williams of the Human Resources and Community Development Division wrote the paper under the direction of Nancy Gordon and Ralph Smith. Paul Cullinan of the Budget Analysis Division prepared estimates of budgetary effects. Roald Euller wrote the computer programs to tabulate extensive data. Paul Cullinan, Richard Kasten, and David Lindeman reviewed various drafts of the paper. Amanda Balestrieri edited the manuscript, and Ronald Moore prepared the paper for publication.

In accordance with CBO's mandate to provide objective analysis, the paper makes no recommendations. Questions should be directed to Roberton Williams of CBO's Human Resources and Community Development Division at (202) 226-2663.

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SUMMARY

This analysis examines two aspects of modifying the Social Security earnings test for people aged 65 through 69: the impact on beneficiaries currently affected by the earnings test of selected options for raising earnings limits, and the budgetary effects of those options. The paper does not consider other factors related to changing the earnings test, such as administrative cost savings from simplifying the test, or the labor supply response of beneficiaries--that is, whether they would choose to work more or less than they do under current law.

In 1988, the earnings test reduces payments to beneficiaries between the ages of 65 and 69 by $1 for each $2 of earnings in excess of the exempt limit of $8,400. The analysis, however, focuses on the effects of the earnings test in 1986, the most recent year for which data are available. In that year, the earnings limit for people aged 65 through 69 was $7,800. In addition, because the analysis is based on data from the Current Population Survey, small differences may exist between the findings of this paper and program statistics from the Social Security Administration.

PEOPLE AFFECTED BY THE EARNINGS TEST

In 1986, more than 8 million people aged 65 through 69 received or were eligible to receive Social Security benefits. (Unless otherwise stated, references are to calendar years.) This number--and all numbers in the analysis of characteristics of people affected by the earnings test--excludes people who appear to have retired during 1986, since available data do not show whether they would have been affected by the earnings test.

Almost one-fifth of potential Social Security recipients aged 65 through 69--nearly 1.6 million people--had some earnings in 1986, but only about 600,000 of them received lower benefits because of the earnings test. This affected group made up less than two-fifths of earners and less than 10 percent of all who were eligible for benefits. They were affected either by payment reductions or because they delayed applying for benefits. (Other beneficiaries may have limited their earnings in order to receive full benefits, but the data necessary to include them in the analysis are not available.)

Those affected by the earnings test were more likely than those not affected:

- to be men;
- to live with their spouses;
- to have family incomes above $32,000; and

- to have family incomes above four times the poverty threshold--that is, above about $21,000 for a single person and about $26,500 for a couple.

Only 1 percent of those affected by the earnings test had family incomes below twice the poverty threshold--that is, below about $10,500 for a single person and about $13,300 for a couple--compared with roughly one-third of all people aged 65 through 69 eligible for Social Security.

EFFECTS OF CHANGING THE EARNINGS LIMIT

This analysis examines the number and characteristics of people who would no longer incur benefit reductions if the earnings limit were raised or eliminated, as well as the increase in budgetary outlays such changes would cause. Because of limitations of the Current Population Survey data, however, the analysis does not show the amounts by which Social Security payments would rise for different groups of recipients. (While changes in benefit levels could be calculated using data from other sources, those other sources lack information on family incomes and living arrangements.) In addition, the analysis of the characteristics of people affected by modifications to the earnings test excludes both recent retirees subject to a monthly earnings test and dependents whose benefits are affected by workers' earnings; these groups are, however, included in estimates of budgetary effects.

The analysis of the characteristics of beneficiaries who would be affected by a modified earnings test does not account for any behavioral changes that might be induced by increasing the earnings limit. A higher limit might cause some Social Security beneficiaries to work more than they now do, and thus to pay additional payroll and income taxes. At the same time, some workers may elect to apply for Social Security benefits earlier than they would under the current earnings test; this would increase benefits currently paid, but reduce future benefits since fewer such workers would receive delayed retirement credits. The aggregate effect of such behavioral shifts is reflected in this study's budgetary estimates.

The analysis examines four possible changes to the earnings test:

- Raise the earnings limit to $10,000 in 1989. A comparable limit (of about $9,000) would have exempted about 85,000 people in 1986, about 14 percent of all those actually affected by the earnings test.

- Double the earnings limit to an estimated $17,280 in 1989. In this case, nearly 270,000 of those affected by the actual earnings test--45 percent--would not have been affected in 1986.

- Raise the earnings limit to $25,000 in 1989. In 1986, a comparable limit (of about $22,560) would have exempted about 375,000 people, nearly two-thirds of those affected under current law.

- Eliminate the earnings test. All 600,000 affected people would have been eligible for higher benefits.

Three conclusions stand out with respect to these four options:

- Gains would go primarily to people with high family incomes. Under each of the options, at least 72 percent of the people made exempt from the earnings test would have incomes greater than three times the poverty level--that is, greater than about $15,800 for a single person and about $19,900 for a couple.

- All four options would focus gains on men living with their spouses in families with incomes greater than four times the poverty level.

- Among those affected by the earnings test, most women, widows and widowers, and people with low family incomes would become exempt if the earnings limit were doubled. In contrast, raising the limit further or eliminating it would focus the additional gains on men, married couples, and people with high family incomes.

Federal budget outlays for Social Security would increase for each of the options over the next five years, but costs would be much higher for the larger changes. For example, raising the earnings limit to $10,000 in 1989 would increase outlays by about $1.3 billion over the 1989-1993 period, but doubling it (to $17,280 in 1989) would cost over six times as much--more than $8 billion over the five-year period. Increasing the 1989 earnings limit to $25,000 would raise outlays by nearly $11 billion over the 1989-1993 period, while eliminating it entirely would cost nearly $24 billion over the same five years.

Because estimating practices used by the Congressional Budget Office rely on a baseline macroeconomic forecast which incorporates projections of aggregate wages and employment, no revenue effects are estimated for the options to change the earnings test. However, when revenue effects have been considered--as they are in the Social Security Administration's estimates--they offset only a small portion of the additional benefit costs.

CHAPTER I
THE CURRENT EARNINGS TEST

This paper deals with two issues concerning possible changes in the Social Security earnings test for people aged 65 through 69: how selected options to raise or eliminate earnings limits would affect recipients whose benefits are currently reduced as a result of the test, and how those changes would affect federal budget outlays for Social Security. The analysis excludes all beneficiaries who retired during the year, and does not take account of possible behavioral responses to the changes. Furthermore, the paper does not consider related effects such as the simplification of administrative procedures.

Before looking at the effects of relaxing or eliminating the earnings test, it is useful to look more closely at the current earnings test and examine the characteristics of those beneficiaries it affects. Moreover, the constraints imposed on this analysis by the limitations of the available data require some explanation.

HOW THE EARNINGS TEST WORKS

In 1988, Social Security recipients aged 65 through 69 are subject to an earnings test that reduces their benefits by $1 for each $2 they earn above the exempt limit of $8,400.1/ A special monthly earnings test applies in the calendar year in which benefits are first received. If a retired worker earns more than the exempt amount, the benefits of all people receiving payments based on the worker's earnings record are subject to the reduction. Excess earnings of dependents and survivors, however, affect only their own benefits and not those of other family members.2/

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1. Beginning in 1990, people aged 65 through 69 will have their benefits reduced by $1 for every $3 in earnings in excess of the exempt limit. While this policy change will not affect which people are subject to the earnings test, for many beneficiaries it will mean higher benefits than they would otherwise get.

   Beneficiaries under age 65 are also subject to the earnings test, but the limit on earnings is lower--$6,120 in 1988. In addition, the rate of benefit reduction for these younger workers is scheduled to remain at $1 for every $2 of earnings over the exempt limit. Beneficiaries are no longer subject to the earnings test once they reach age 70.

2. The impact of the earnings test is actually somewhat more complicated than this simplified description indicates. In particular, if total family benefits are limited by the maximum family benefit, some members may be able to earn more than the exempt amount without reducing Social Security payments to the family.

Three groups of workers and their families are affected by the earnings test. The main group is Social Security beneficiaries with earnings above the relevant exempt amount. This group includes both those who get no Social Security payments because the reduction caused by the earnings test exceeds their benefit level, and those who get smaller--but still positive--benefits.

A second group includes workers who delay their application for Social Security benefits. This situation may occur because such people want or need to continue working and either expect their benefits to be fully withheld under the earnings test--and thus do not bother to apply--or do not want to have their Social Security payments reduced.3/

The third group of affected people is Social Security recipients who limit their earnings so that their benefits are not reduced. Some of these people elect not to work at all, while others work fewer hours than they would otherwise to hold their annual earnings below the exempt amounts.

Retired workers whose earnings over the exempt limit cause them to lose benefits are compensated either through the delayed retirement credit--which increases benefits by 1/4 percent for each month in which benefits are reduced--or through a reversal of the early retirement reduction.4/ If these two factors were fair on an actuarial basis, the earnings test would simply defer benefits;

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3. As discussed in the next footnote, people who have benefits withheld because of the earnings test receive future benefits that are higher than they would otherwise be. Whether or not such adjustments are actuarially fair, beneficiaries may perceive the loss of benefits through the earnings test to be permanent, and thus fail to apply for benefits.

4. Benefits are reduced by 5/9 percent for each month under age 65 that a worker is when he or she first receives Social Security old age benefits. Before the worker's 65th birthday, for each month in which benefits are withheld because of the earnings test, one month's early retirement reduction is restored. Once the worker turns 65, the delayed retirement credit increases benefits by 1/4 percent in 1988--rising to 2/3 percent for people who turn age 62 in 2005 and after--for each month in which the earnings test causes benefits to be partially or fully withheld.

higher future benefits would, on average, offset the value of reduced current benefits.5/

Analysts claim that although the early retirement reduction is approximately actuarially fair, the current delayed retirement credit is too low, so the earnings test now imposes a long-run penalty. In fact, the delayed retirement credit is slowly being raised to 2/3 percent per month for people who turn age 62 in 2005 and later years, after which it too should be close to actuarially fair. Once that is the case, the earnings test will serve only to shift the timing of benefit payments--and hence, of federal expenditures--into the future.

Any individual's experience may nevertheless be better or worse, since an actuarially fair adjustment is only fair on average. Some people will lose benefits because they die earlier than expected, while others will gain because they live longer. To the extent that there is adverse selection among those deciding to retire early or work longer--that is, people in worse health retire early and those in better health work longer--this situation is exacerbated: the less healthy early retirees may die at younger ages and thus suffer disproportionately greater losses, while the healthier late retirees may live longer and receive even greater benefits.

Another factor that influences the effects of the earnings test is the taxation of Social Security benefits for people with incomes above fixed limits. (Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.) Up to half of Social Security income is taxable if the sum of one-half of Social Security and Railroad Retirement income plus all of adjusted gross income and tax-exempt interest exceeds $25,000 for single people or $32,000 for married couples filing jointly. Because those with higher incomes must pay taxes on half of their Social Security benefits, the net impact of having those benefits withheld because of the earnings test is less than it would otherwise be. Furthermore, to the extent that their incomes will be lower when their earnings drop below the earnings test limit, recipients may be subject to lower tax rates when they do receive their higher benefits in the future.

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5. This is true by definition: benefit adjustments are actuarially fair if forgone (or additional) payments today are equal, on average, to the present value of expected additional (or reduced) benefits in the future. Future benefits are adjusted even if only part of a month's payment is withheld because of the earnings test. While such adjustments somewhat overcompensate for partial withholding, this would not be expected to have a major effect on actuarial fairness.

Proponents of easing or eliminating the earnings test assert that Social Security is primarily a pension for which workers have paid through payroll taxes, and that it is unfair to penalize those who continue to work. They point to the high effective marginal tax rates on earnings for those subject to benefit reductions: in addition to the 50 percent tax imposed by the earnings test, workers with taxable incomes in the lowest tax bracket also pay 15 percent in federal income taxes and 7.51 percent in Social Security and Medicare taxes--a total marginal tax rate of more than 72 percent --plus any state and local income and payroll taxes, during the phase-out range of their Social Security benefits.6/ Besides this adverse impact on recipients, critics point to the administrative complexity which the earnings test imposes: beneficiaries are required to file annual statements of expected earnings, and the Social Security Administration must adjust payments, credit workers' records with their additional earnings, apply delayed retirement credits, and correct retroactively for over- and underpayments, all at significant expense. (The Social Security Administration estimates that retroactive correction of mispayments is required for 80 percent of people who have benefits withheld because of the earnings test.)

Proponents of retaining the current earnings test base their support on the belief that the major purpose of Social Security is to replace earnings lost as a result of retirement, death, or disability. To the extent that beneficiaries continue to have substantial earnings, they argue, there is less need for replacement and benefits should be reduced. Furthermore, they dispute the claim that Social Security is a pension, arguing that the benefit structure--paying relatively more to those with low earnings than to those with high earnings, and providing rates of return on contributions much higher than private pensions, at least for current retirees--is unlike that of pensions.

DATA AND LIMITATIONS OF THE ANALYSIS

This analysis is based on data from the March 1987 Current Population Survey (CPS), which contains information about incomes received during calendar year 1986. While this is the most recent year for which such data exist, 1986 may not provide an accurate representation of economic conditions today or in the future. In particular, the overall civilian unemployment rate in 1986 was 7.0 percent, but it is projected by the Congressional Budget Office (CBO) to be significantly lower in 1988 and subsequent years. It is uncertain how the current tight labor markets affect the employment of the elderly, but the increased availability of jobs may induce more elderly people to work. In light of these facts,

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6. In 1990, when the benefit reduction in the earnings test falls to one-third, this marginal tax rate will drop to about 56 percent, plus any state or local tax rates.

some caution is in order in using these findings to predict the future. In 1986, the exempt earnings limit for beneficiaries between the ages of 65 and 69 was $7,800.7/

Unfortunately, the limitations of these data from the CPS impose two constraints on the analysis. First, because respondents report their eligibility for Social Security only if they received payments during the year, the analysis cannot identify either those whose benefits are completely withheld because of high earnings or those who have not yet applied for benefits. Because there is little information to determine which people not reporting Social Security income are eligible to receive payments, the analysis assumes that all people aged 65 through 69 who had earnings were eligible.8/ This assumption imputed eligibility for roughly 250,000 people.

A second constraint exists because the CPS does not indicate the amount of Social Security beneficiaries would receive if their payments were not reduced by the earnings test. The amounts reported on the CPS may be before or after reductions, or they may include lump-sum adjustments--either reductions or repayments--based on Social Security actions in previous years. Because recipients' basic benefit levels are unknown, CBO cannot estimate how much individual benefits are reduced because of the earnings test. As a result, the analysis is limited to examining the characteristics of people affected by the current earnings test and of those who would no longer be affected if the earnings test limit were raised or eliminated. In addition, it is impossible to determine whether a worker's earnings in excess of the earnings limit affect benefits payable to his or her dependents; consequently, such dependents are omitted from the examination of the characteristics of people affected by the earnings test.

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7. The earnings limit is indexed to the national average of wages reported to the Social Security Administration on W-2 tax forms. Such indexing applies, however, only when the average wage rises; the law precludes any reduction in the earnings limit. Recent limits have been:

1983	$6,600	1986	$7,800
1984	$6,960	1987	$8,160
1985	$7,320	1988	$8,400

CBO projects the limit to be $8,640 in 1989 and $9,120 in 1990.

8. Some of these people might have received benefits but inaccurately reported on the CPS that they did not. This might be particularly likely in the case of dependents, for whom benefits might be lumped in with a retired worker's payments.

A third limitation on the analysis concerns changes in the behavior of beneficiaries. Because it is not known how individuals would respond if the earnings test were changed, the analysis of the characteristics of people who would be affected by modifying the test does not take account of any behavioral responses that might result. Two kinds of responses might be expected. First, some Social Security recipients might choose to change the amount they work if the exempt limit on earnings were raised. Some might work more because their effective tax rates were reduced, while others --with earnings above current limits--might work less because their Social Security payments increased. As a result, both payroll and income tax revenues could change. Second, some workers who now postpone applying for benefits because of high earnings might choose to apply earlier. This would cause an increase in benefits currently paid, but future payments would be lower than otherwise since some such workers would not receive delayed retirement credits. The effect of such responses would probably not be large, relative to the direct effects of changing the earnings test.

Because of the data limitations, the analysis is based on about 600,000 people aged 65 through 69 whose benefits were reduced or completely withheld in 1986--or who did not apply for benefits--as a result of the earnings test (see Table 1). It excludes, however, those people who appear to have retired during 1986.9/ (This exclusion was necessary because it is not possible to determine which recent retirees were affected by the earnings test; those who retire during a year are subject to a monthly earnings test in that year, and the CPS does not report monthly earnings data.) As a result, the analysis understates slightly the full impact of the earnings test on this age group.

This population group--people aged 65 through 69 eligible to receive Social Security payments, excluding recent retirees--is the basis for the analysis of characteristics of people affected by the earnings test and modifications to the test. This population is referred to as beneficiaries or insured people.

PEOPLE AFFECTED BY THE EARNINGS TEST IN 1986

Fewer than one in ten people aged 65 through 69 who are eligible for Social Security benefits is affected by the earnings test, and the characteristics of those affected are quite different from those of the average beneficiary.

As would be expected, beneficiaries with earnings above the exempt limit tend to have higher family incomes: while only about

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9. The analysis excluded Social Security beneficiaries who reported that they worked during 1986 and that they were retired in March 1987. This approach can only roughly identify recent retirees subject to the monthly earnings test.

TABLE 1. REPORTED AND IMPUTED SOCIAL SECURITY ELIGIBILITY IN 1986 OF PEOPLE AGED 65-69 WITH EARNINGS ABOVE $7,800

Population Subgroup	Number (In thousands)	Distribution of Affected People (In percent)
Annual earnings above $7,800 and reporting Social Security benefits		
Men	215	36
Women	168	28
Men and Women	383	65
Annual earnings above $7,800 and not reporting Social Security benefits		
Men	156	26
Women	55	9
Men and Women	211	35
Total		
Men	370	62
Women	223	38
Men and Women	594	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: Details may not add to totals because of rounding.

one-eighth of all beneficiaries had family incomes in 1986 above $42,000, more than 40 percent of those affected by the earnings test had incomes above that level (see Figure 1, and Table A-1 in Appendix A).10/ In contrast, nearly 40 percent of all beneficiaries had incomes below $15,000, compared with only 5 percent of people with earnings above the exempt limit. Because beneficiaries had to have more than $7,800 in income from earnings to be affected by the earnings test, those affected would almost certainly have higher total incomes than beneficiaries on average. Thus, virtually no affected people would have had extremely low incomes.

Because men are more likely both to work and to have higher earnings when they do work, they are significantly more likely to be affected by the earnings test than are women. In 1986, 11 percent of men eligible for Social Security had earnings above the exempt limit, compared with just 5 percent of women. Furthermore, among those affected by the earnings test, men tended to have higher incomes than women: more than half of affected men but just one-fourth of affected women had incomes above $42,000.

Family income does not take into consideration the varying needs due to differences in family size, and using such a measure may therefore give an inaccurate assessment of the well-being of people affected by the earnings test. An income of $20,000 might allow one person to live quite well, for instance, but would not go as far for a family of four. Poverty thresholds reflect the differential needs of families of various sizes, so measuring income relative to the appropriate poverty threshold may be a better indicator of well-being. Such a measure would indicate, for example, that a single person with an income of $10,000 would be roughly as well off as a family of four with an income of $20,000.11/

There are separate poverty thresholds for elderly and nonelderly families with one or two members. In 1986, the poverty threshold for a single person age 65 or over was $5,255, about 8 percent below the $5,701 threshold for a single person under age 65. Similarly, a two-person family headed by a person aged 65 or over had a 1986 poverty threshold of $6,630, compared with $7,372 for a younger two-person family, a difference of roughly 10 percent. Because this analysis looks only at people aged 65 through 69, the

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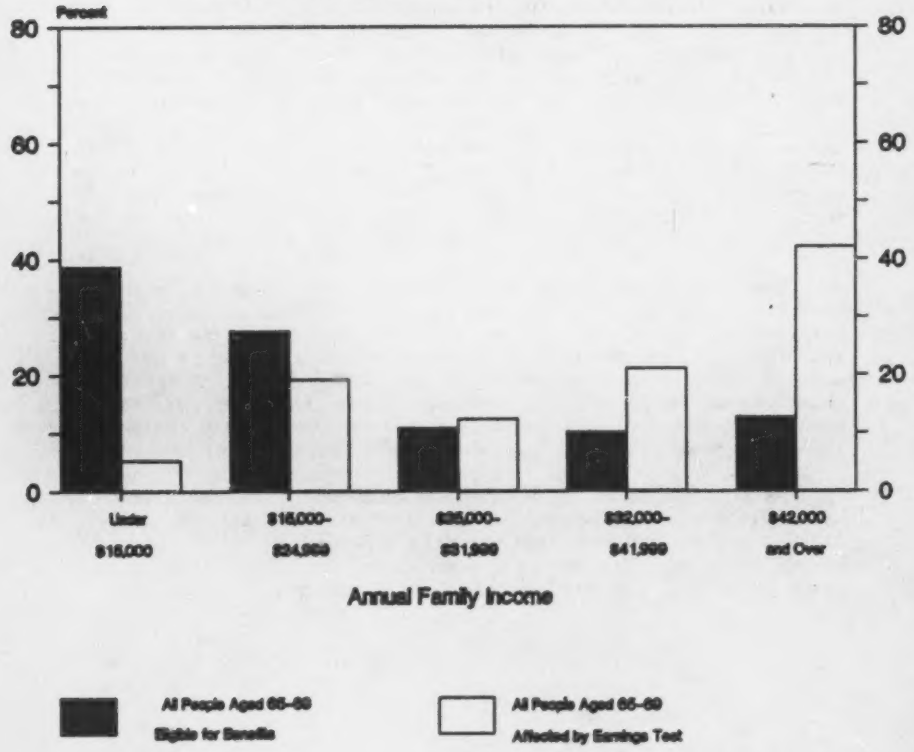
10. Appendix A provides detailed statistics on the characteristics of people aged 65 through 69 eligible for Social Security in 1986, those affected by the earnings test in 1986, and those who would not have been affected in 1986 had there been a higher or no earnings limit.

11. For a more complete discussion of this approach to measuring well-being, see Congressional Budget Office, Trends in Family Income: 1970-1986 (February 1988), pp. 5 and 6.

FIGURE 1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

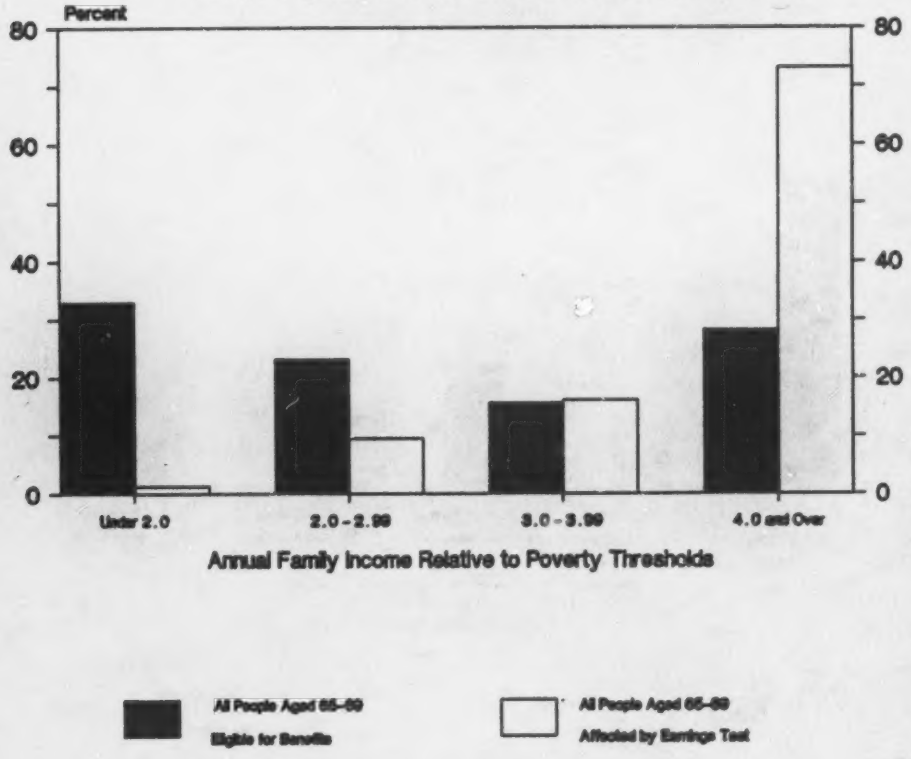
lower thresholds for the elderly are used. Poverty thresholds for families with three or more members are the same for both age groups.

Measuring income relative to poverty provides further evidence that the earnings test affects primarily those who are economically better off. In 1986, while beneficiaries with family incomes above four times the poverty threshold--that is, more than about $21,000 for people living alone and about $26,500 for couples--made up just over one-fourth of all beneficiaries, they constituted nearly three-fourths of those affected by the earnings test (see Figure 2, and Table A-2 in Appendix A). Conversely, those with incomes below twice the poverty threshold--that is, about $10,500 for single people and about $13,300 for couples--represented one-third of all beneficiaries but barely 1 percent of those with earnings above the exempt level. Again, men were better off than women: over 80 percent of affected men had family incomes more than four times the poverty threshold, compared with 60 percent of affected women.

The distribution among living arrangements of people affected by the earnings test in 1986 was generally similar to that of all beneficiaries, although this was less true for women (see Figure 3, and Table A-3 in Appendix A). Seven out of ten affected people were married, and 80 percent of those couples lived by themselves. Relative to their numbers, married women eligible for Social Security benefits were less likely to have earnings above the exempt limit than their never-married, divorced, or separated counterparts.

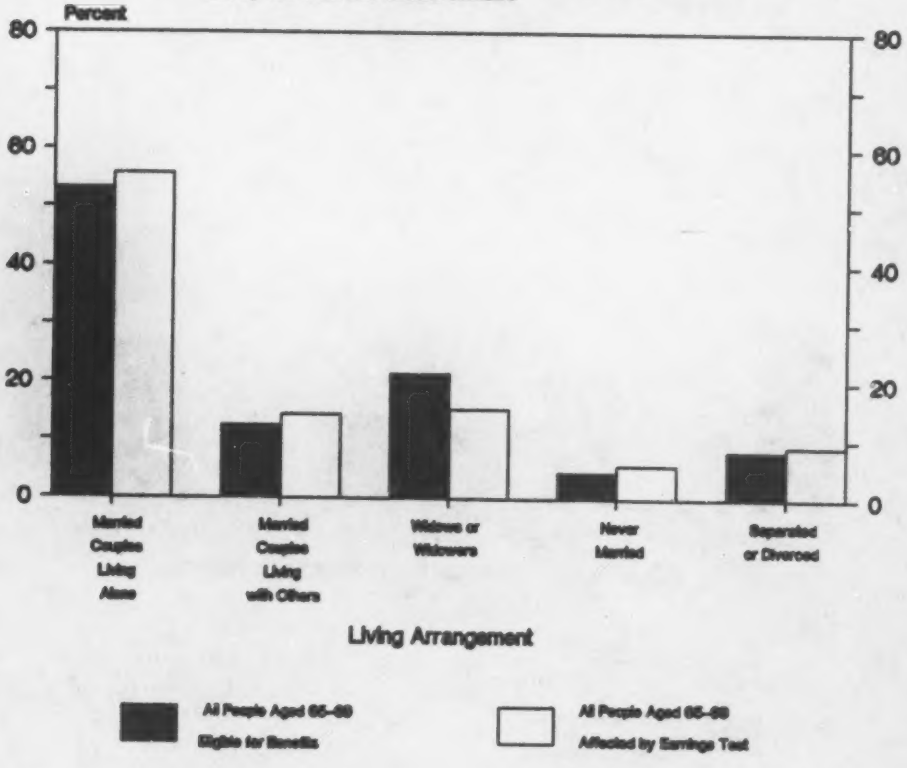
As Figure 4 shows, only 1 percent of people with family incomes below $15,000 and 5 percent of those with family incomes between $15,000 and $25,000 had their benefits reduced because of earnings. Virtually no one affected by the earnings test had a family income below twice the poverty threshold (see Figure 5).

FIGURE 2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



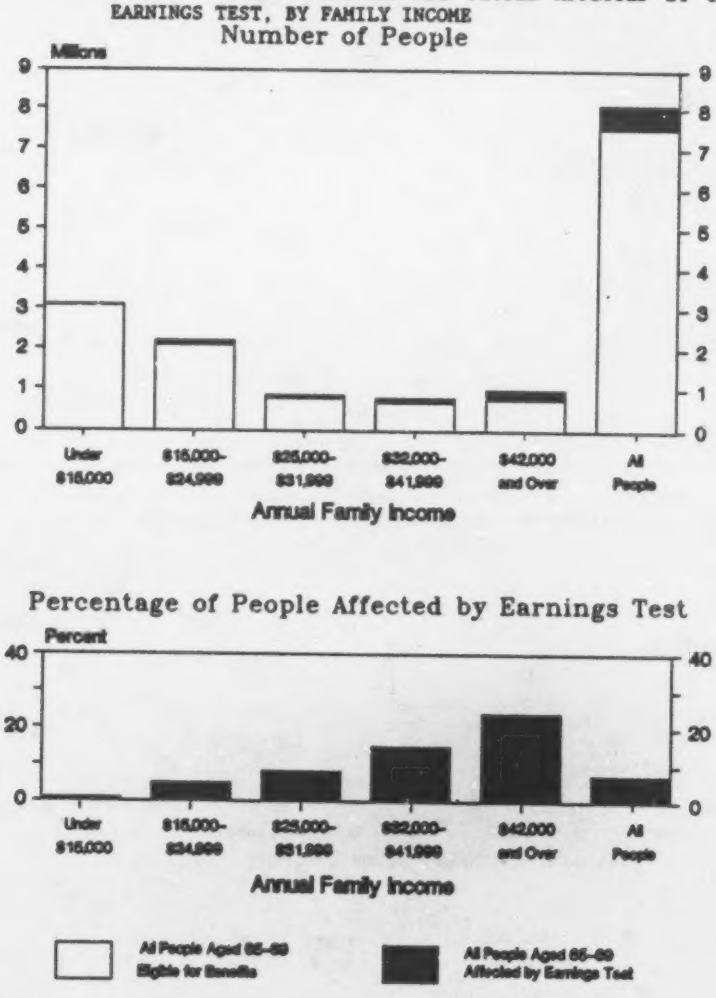
SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

FIGURE 3. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY LIVING ARRANGEMENT



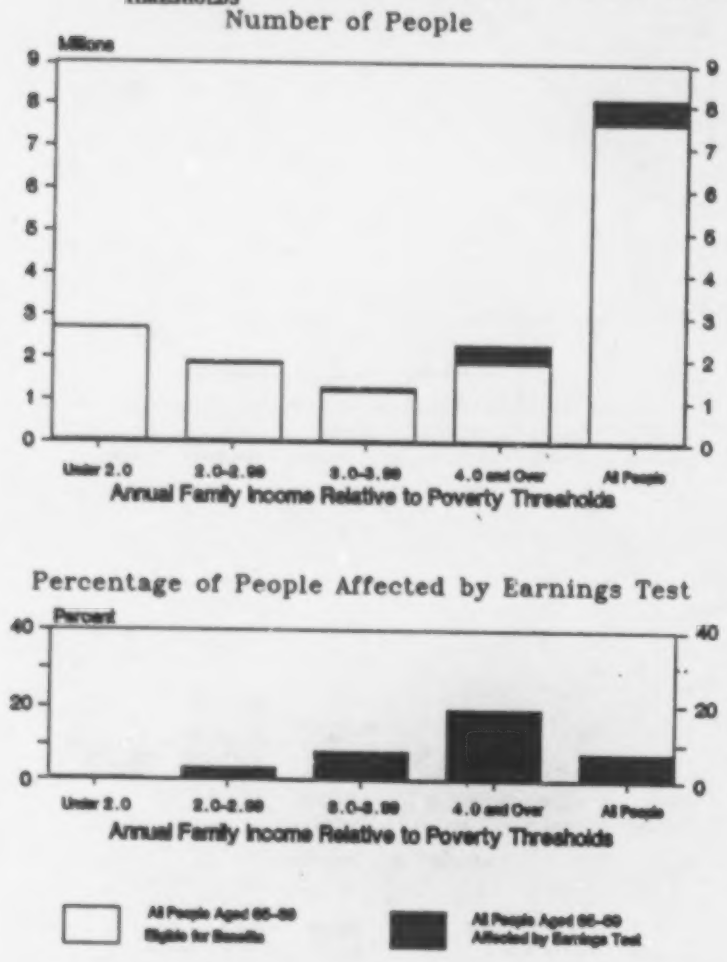
SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

FIGURE 4. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND PEOPLE AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME



SCURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

FIGURE 5. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND PEOPLE AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

CHAPTER II
EFFECTS OF CHANGING THE EARNINGS LIMIT

Proposals currently before the Congress would increase the Social Security earnings limit or eliminate it entirely for beneficiaries aged 65 through 69. This analysis examines four possible changes:

- Increase the earnings limit to $10,000 in 1989, thereby raising it 16 percent from the estimated $8,640 limit for 1989;
- Double the earnings limit to $17,280 in 1989;
- Raise the 1989 earnings limit to $25,000, that is, to three times the estimated limit under current law; and
- Eliminate the earnings test for people between 65 and 69 years of age.

Each of the options that would increase the exempt earnings amount would resume the current law wage indexing of the threshold in 1990.

The characteristics of people who would be affected by these options were simulated using 1986 data on incomes from the March 1987 Current Population Survey. To make the 1986 limits comparable, the 1989 limits given above were deflated based on the past and projected growth in the average wage. The equivalent limits used with the 1986 data were $9,000, $15,600, $22,560, and none, respectively.

WHICH GROUPS WOULD BE AFFECTED?

Raising the earnings limit would exempt some people who are now affected--those with earnings above the current limit but below the new limit--from benefit reductions because of the earnings test. The size of this group obviously depends on how much the earnings limit is raised: a small increase, such as in the first option, would exempt relatively few people, while eliminating the earnings test entirely would make everyone exempt. Available data on earnings identify people in this group, but the amounts by which their Social Security payments would rise cannot be determined without information on benefit levels.

Among those who would still be affected by the earnings test after the earnings limit was raised (but not eliminated), some beneficiaries would get higher payments while others would not. People with high earnings relative to their primary insurance amounts--that is, their unadjusted benefits--would be likely to have their benefits fully withheld under both the current and new earnings limits, and would thus gain nothing from an increase in the earnings limit. Others whose earnings are lower relative to their primary insurance amounts and whose benefits are now at least partly withheld could have less of their benefits withheld after the change and thus would gain.

Unfortunately, without information on primary insurance amounts, the analysis can identify only those people who would become exempt from benefit reductions as a result of a change in the earnings test. Among those beneficiaries still affected by the test, those who would gain cannot be distinguished from those who would not.1/ The remainder of the analysis therefore provides information only about those people who would no longer be affected if the earnings test were modified. If those people still affected by the earnings test could be included, the numerical results of the analysis would be different, but the qualitative results would be highly unlikely to change.

WHICH BENEFICIARIES WOULD BE MADE EXEMPT?

The analysis next focuses on the characteristics of people aged 65 through 69 who would no longer be affected by the earnings test if the exempt earnings limits were increased. Three terms are used to refer to different population groups. "Insured" people are those 65-to-69-year-olds who are eligible to receive Social Security, whether or not they actually get benefits. "Affected" people are those insured people whose benefits are partially or fully withheld because of the current earnings test; this group includes those who get no benefits and whose earnings are above the exempt limit. "Exempted" people are those affected by the current earnings test who would no longer be affected if the test were changed.

If the 1986 earnings limit had been raised from $7,800 to $9,000, 85,000 insured people aged 65 through 69--14 percent of those affected by the earnings test in 1986--would have become exempt from the earnings test and an indeterminate number of others would have received increased Social Security checks (see Figure 6, and Table A-4 in Appendix A). Doubling the limit to $15,600 would have exempted more than three times as many people--nearly 270,000 or 45 percent of those affected by the earnings test. A still larger increase to $22,560 would have reduced the number of people affected by the earnings test by almost two-thirds, or about 375,000. Of course, eliminating the earnings test would have exempted all 600,000 people whose benefits were reduced or fully withheld in 1986 because of excess earnings.

Small increases in the earnings limit would exempt a large fraction of affected beneficiaries in low-income families, but would leave most people with higher family incomes still affected by the earnings test (see Figure 7). About half of affected people in

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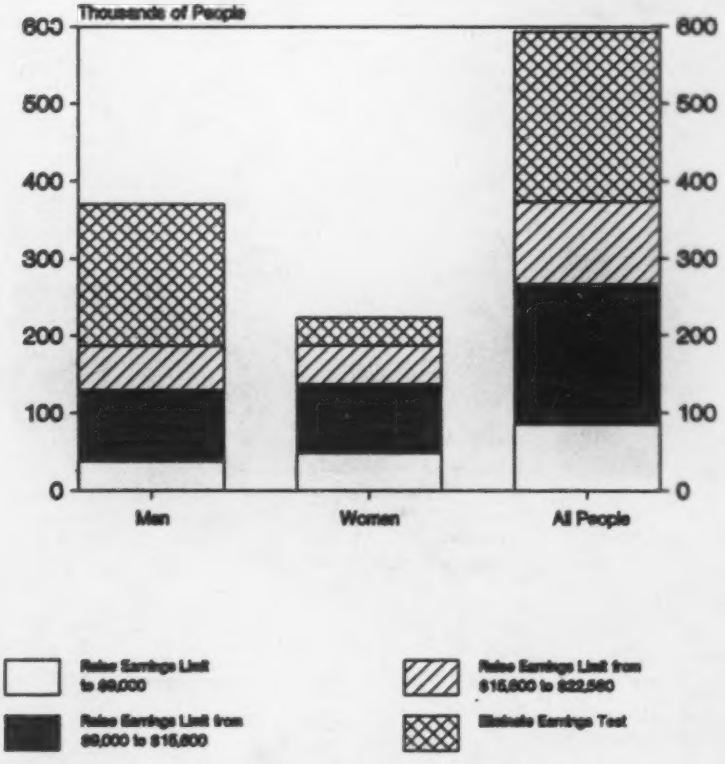
1. Without information on individual Social Security benefit levels before the earnings test is applied, the analysis cannot determine either the amount by which individual Social Security payments would rise if earnings limits were increased or the earnings levels of individuals at which benefits would become fully withheld.

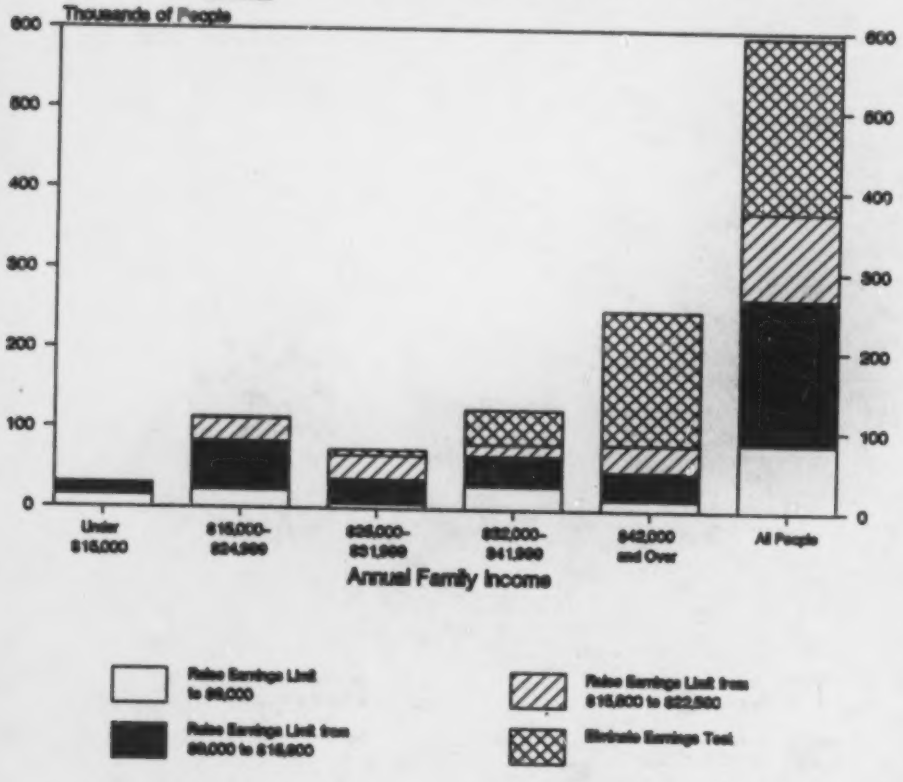
FIGURE 6. PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST IN 1986 AS A RESULT OF SELECTED CHANGES, BY SEX



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The effects of changing the earnings test shown in the figure are cumulative. For example, the number of people made exempt by doubling the earnings limit equals the number exempted by raising the limit to $9,000--the unshaded box--plus the incremental group exempted when the limit is further raised to $15,600--the black box.

FIGURE 7. PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST IN 1986 AS A RESULT OF SELECTED CHANGES, BY FAMILY INCOME



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The effects of changing the earnings test shown in the figure are cumulative. For example, the number of people made exempt by doubling the earnings limit equals the number exempted by raising the limit to $9,000--the unshaded box--plus the incremental group exempted when the limit is further raised to $15,600--the black box.

families with annual incomes below $15,000 would not have been subject to benefit reductions if the earnings limit had been $9,000 in 1986. In contrast, such a change would have exempted only about 5 percent of affected people with family incomes above $42,000. Even if the earnings limit had been tripled, fully two-thirds of people with incomes in that top category would have been affected by the earnings test in 1986.

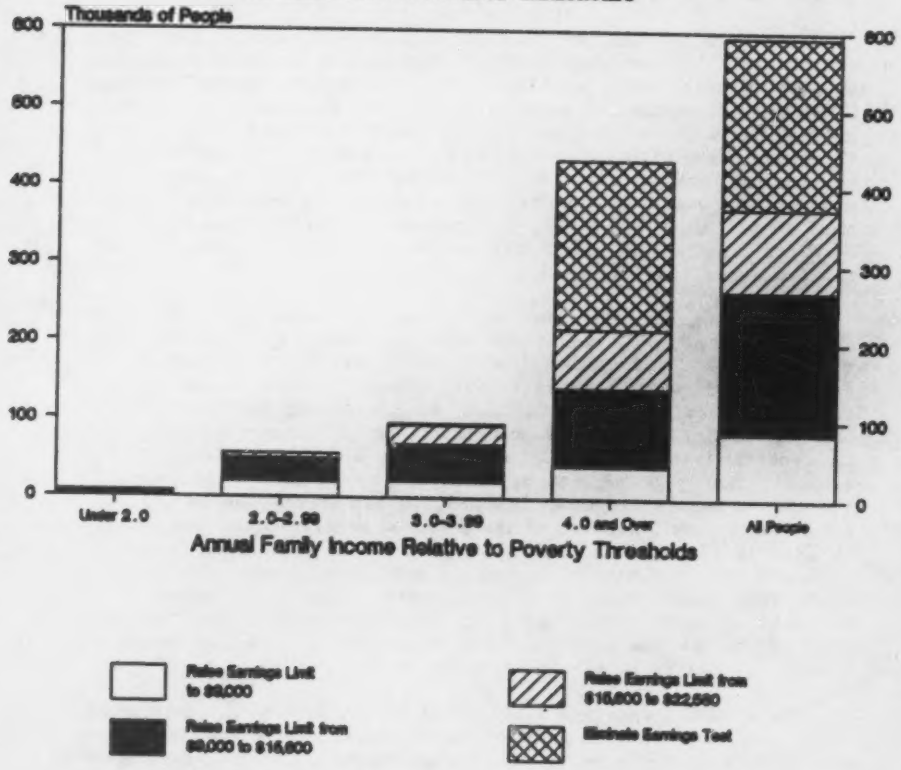
That smaller changes have significant effects on low-income beneficiaries is even more apparent when income is measured relative to poverty thresholds (see Figure 8). A doubling of the earnings limit in 1986 would have exempted virtually all people with family incomes below three times the poverty threshold, but left about two-thirds of those with incomes above four times the poverty threshold subject to benefit reductions. Furthermore, because widows and widowers and women who have never married tend to have lower incomes than people in other living arrangements, smaller changes in the earnings limit exempt relatively more widows and widowers and never-married women (see Figure 9).

Examining the distribution across recipient groups of those who would be made exempt by each of the four options both supplements and reinforces this picture. Smaller increases in the earnings limit would have relatively greater effects on people with low family incomes than would larger increases, but none of the changes examined would have much impact on low-income beneficiaries in general (see Figure 10, and Table A-5 in Appendix A). For example, nearly 20 percent of those who would have been exempt if the 1986 earnings limit had been $9,000 had incomes below $15,000, even though just 5 percent of all affected beneficiaries had incomes at that level. The data also imply, however, that even under the smallest increase in the earnings limit, only a small fraction of those made exempt would have low incomes: less than half would be in families with incomes below $25,000. A similar pattern appears when income is measured relative to the poverty thresholds (see Figure 11, and Table A-6 in Appendix A).

Raising the earnings limit to $9,000 in 1986 would have meant that a disproportionate share of the exempted population would have been widows or widowers, or people who had never married (see Figure 12, and Table A-7 in Appendix A). To a large extent, this reflects the relative distribution of earnings among people with different living arrangements. For example, while they constituted 22 percent of insured people and 15 percent of affected people in 1986, widows and widowers would have made up 27 percent of those exempted by changing to a $9,000 limit. In contrast, higher or no earnings limits would have meant that larger shares of those exempted would have been married couples.

An examination of men and women separately across living arrangements and income levels reinforces the preceding observations. Appendix B provides information about the distributions--by all

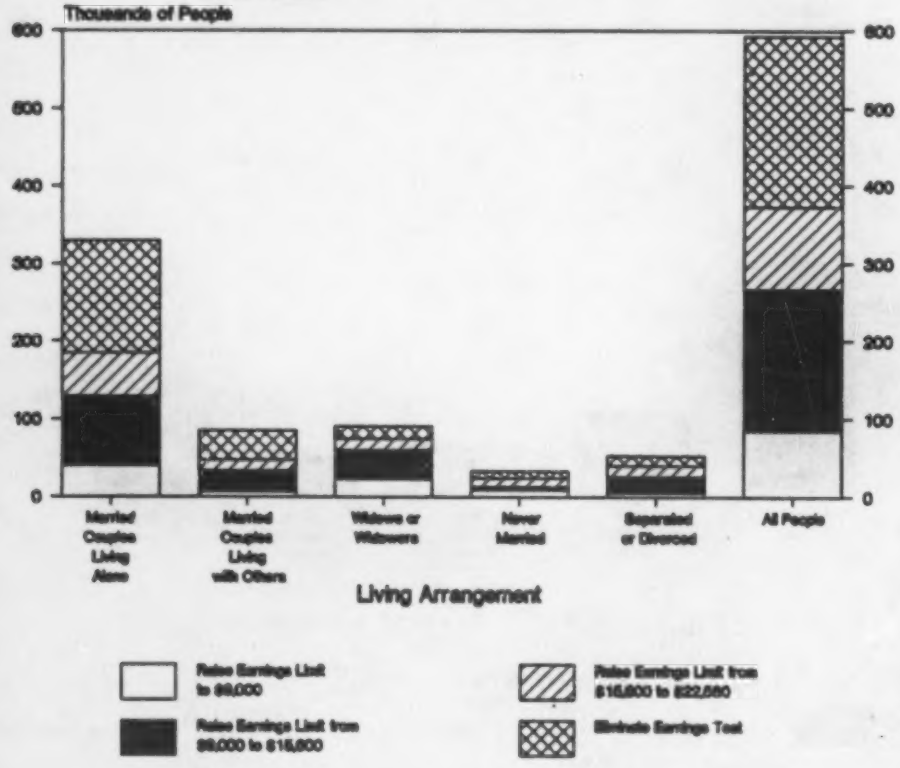
FIGURE 8. PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST IN 1986 AS A RESULT OF SELECTED CHANGES, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The effects of changing the earnings test shown in the figure are cumulative. For example, the number of people made exempt by doubling the earnings limit equals the number exempted by raising the limit to $9,000--the unshaded box--plus the incremental group exempted when the limit is further raised to $15,600--the black box.

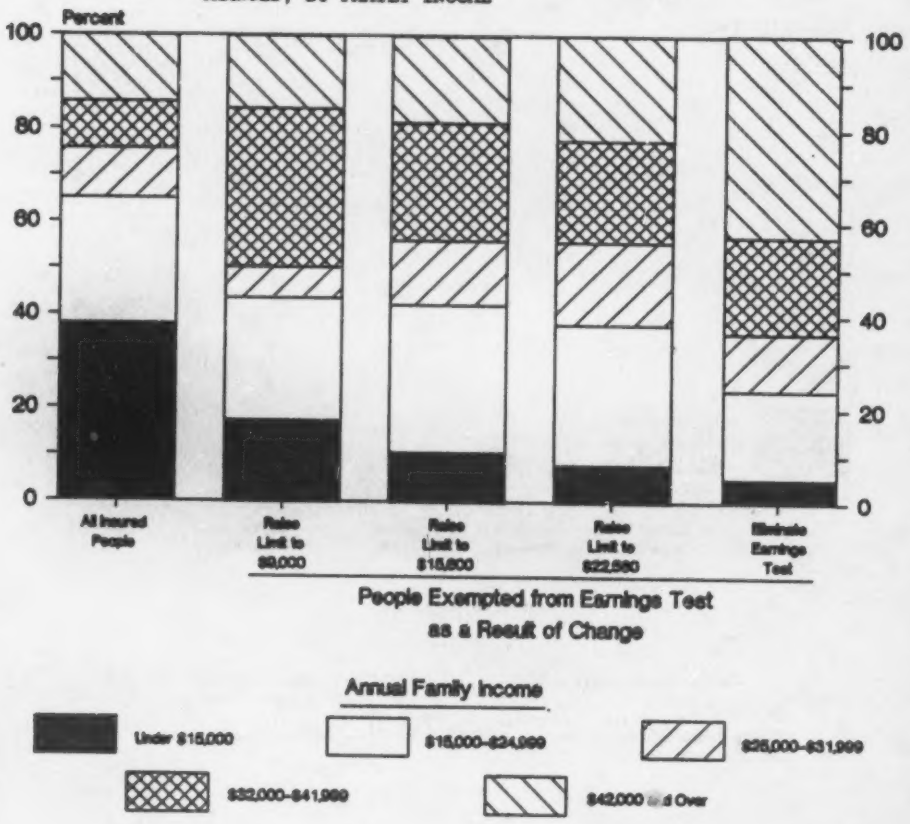
FIGURE 9. PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST IN 1986 AS A RESULT OF SELECTED CHANGES, BY LIVING ARRANGEMENT



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The effects of changing the earnings test shown in the figure are cumulative. For example, the number of people made exempt by doubling the earnings limit equals the number exempted by raising the limit to $9,000--the unshaded box--plus the incremental group exempted when the limit is further raised to $15,600--the black box.

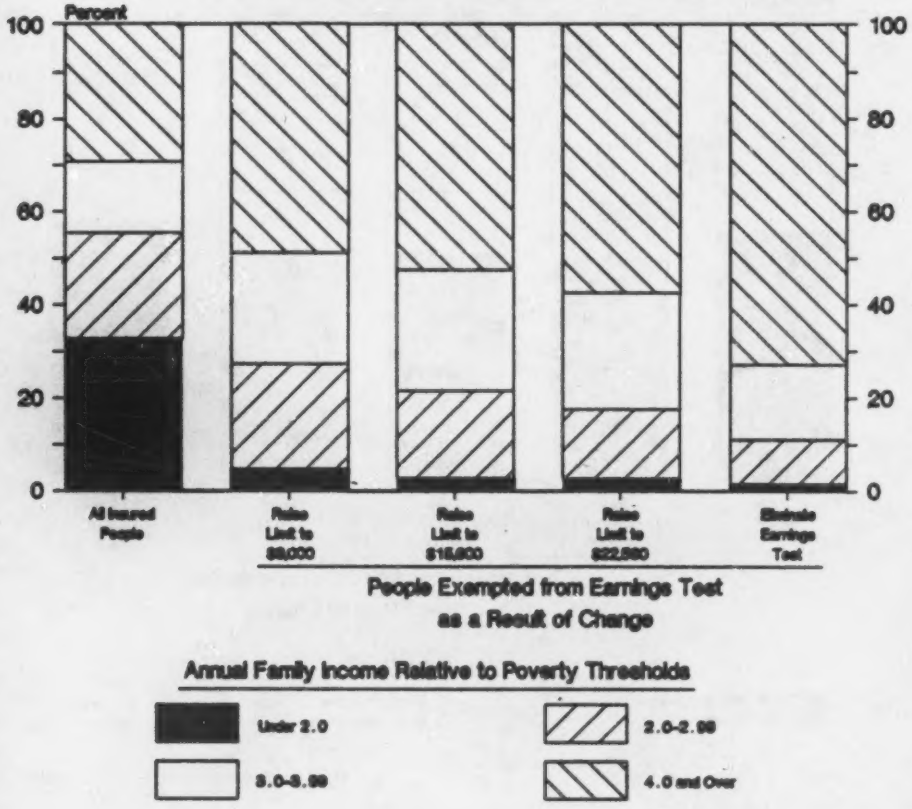
FIGURE 10. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST AS A RESULT OF SELECTED CHANGES, BY FAMILY INCOME



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The distribution of people no longer affected if the earnings test was eliminated is the same as the distribution of all people affected by the earnings test.

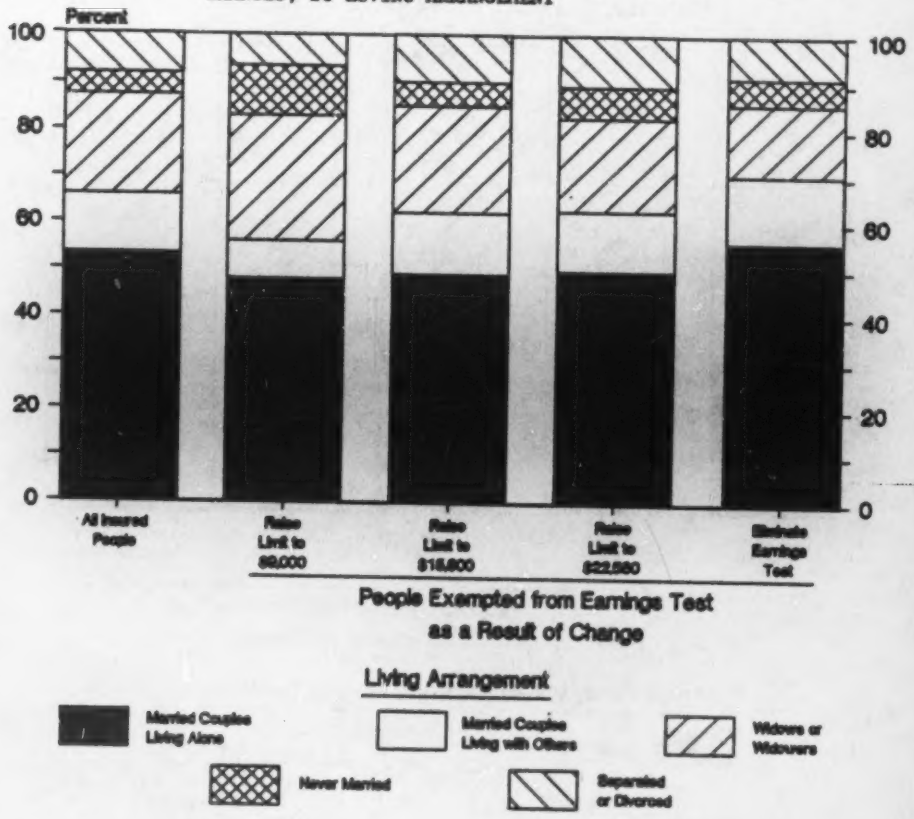
FIGURE 11. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST AS A RESULT OF SELECTED CHANGES, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The distribution of people no longer affected if the earnings test was eliminated is the same as the distribution of all people affected by the earnings test.

FIGURE 12. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 NO LONGER AFFECTED BY THE EARNINGS TEST AS A RESULT OF SELECTED CHANGES, BY LIVING ARRANGEMENT



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: The distribution of people no longer affected if the earnings test was eliminated is the same as the distribution of all people affected by the earnings test.

combinations of sex, family income relative to poverty thresholds, and living arrangement--of the entire eligible population aged 65 through 69, as well as the groups who would have been exempt from the earnings test in 1986 under each of the options for change. Relative to all insured people (see Table B-1), those who would be made exempt by any of the four changes are less likely to have incomes below twice the poverty threshold and more likely to have incomes above four times the poverty threshold, regardless of living arrangement.

At the same time, the smaller of the four changes would focus gains--in terms of the number of people exempted--on women, widows, and those with low incomes. Again, this finding results primarily from the distribution of earnings among groups: women, widows, and people in low-income families are more likely to have low earnings. For example, about 11 percent of people exempted by the smallest change--from $7,800 to $9,000--in the earnings limit in 1986 would have been widows with family incomes below three times the poverty threshold, even though they made up just 3.5 percent of the affected group. Conversely, about 17 percent of people exempted by the smallest change would have been married couples living alone with incomes above four times the poverty threshold, a group that made up roughly 34 percent of all affected people in the 65-69 age group.

These findings can only describe people who would no longer have any benefit reductions because of the earnings test. The amounts by which individual benefits would rise cannot be established. Moreover, it is clear that significant gains would also accrue to people whose benefits would still be partially reduced. Finally, this part of the analysis omits any behavioral responses of people who might choose to work more or to begin receiving benefits earlier if the earnings test limit were raised.

EFFECTS ON FEDERAL OUTLAYS

Each of the options for relaxing or eliminating the earnings test would result in higher Social Security expenditures over the projection period. Unlike the analysis provided elsewhere in this paper, these estimates incorporate certain behavioral responses to changes in the earnings test. The response most important for the budget estimates provided here is the effect these changes may have on applications for cash benefits by those who currently delay applying for benefits because of the earnings test.

Table 2 displays the effects on federal outlays of the four options discussed in this paper for altering or eliminating the earnings test for those aged 65 through 69. Raising the earnings limit to $10,000 in 1989 would increase outlays by about $1.3 billion during the 1989-1993 period, while doubling it--to $17,280 in 1989--would cost more than $8 billion over the same five-year period, about six times as much. If the 1989 earnings limit were raised to $25,000, outlays would increase by about $11 billion for

TABLE 2. EFFECTS ON OUTLAYS OF OPTIONS FOR CHANGING THE SOCIAL SECURITY EARNINGS TEST, 1989-1993 (By fiscal year, in billions of dollars)

Option	1989	1990	1991	1992	1993	Total, 1989-1993
Raise 1989 earnings limit to $10,000 for people aged 65 through 69	0.2	0.3	0.3	0.3	0.3	1.3
Double 1989 earnings limit to $17,280 for people aged 65 through 69	1.2	1.7	1.7	1.7	1.8	8.2
Increase 1989 earnings limit to $25,000 for people aged 65 through 69	1.7	2.4	2.3	2.3	2.3	11.0
Eliminate earnings test for people aged 65 through 69	3.7	5.1	5.0	5.0	5.1	23.9

SOURCE: Congressional Budget Office estimates.

NOTE: Estimates assume implementation of each option on January 1, 1989, and incorporate the effects of additional applications for Social Security benefits.

Details may not add to totals because of rounding.

the 1989-1993 period. Eliminating the earnings test entirely would be by far the most expensive option, costing nearly $24 billion between 1989 and 1993.

Information from the Social Security Administration's (SSA) Office of the Actuary indicates that between 600,000 and 700,000 retired workers aged 65 through 69 have filed for benefits and have some or all of their benefits withheld under the earnings test. In addition, the SSA estimates that 120,000 workers in this age range who have earnings in excess of the exempt amount have not filed for benefits for which they would be eligible if there were no earnings test. The elimination of the earnings test is assumed to induce 90 percent of these workers to file applications for cash benefits. In addition to the retired worker beneficiaries, the SSA estimates that about 150,000 to 200,000 survivors, spouses, and children would receive extra benefits. In total, 900,000 to 1,000,000 persons would be expected to receive additional benefits under a proposal to eliminate the earnings test for the 65-69 age group.

Estimates of outlays resulting from the increases in the exempt amounts are derived from the outlay estimates for the elimination of the test and from the expected changes in who would receive benefits described above. Analysis by the SSA's Office of the Actuary indicates that a tripling of the exempt earnings level would cost slightly less than one-half as much as eliminating the earnings test, while doubling the threshold would generate about one-third of the costs.

Many proponents of relaxing or eliminating the earnings test view these proposals as a mechanism that would encourage the elderly to work more. While the potential effects of the proposed changes could theoretically cause the work of older beneficiaries to increase, decrease, or remain about the same, changes in the labor supply would have a negligible effect on federal outlays, but could raise federal income and payroll tax revenues slightly. For example, the SSA's estimates for eliminating the earnings test assume that new revenues would offset 10 percent to 15 percent of the additional outlays. While most of the increased revenue would come from the income taxes paid on the additional benefit payments, a portion would be the higher payroll and income taxes resulting from increased work by beneficiaries. Under estimating practices used by the Congressional Budget Office, however, the budgetary effects of legislative proposals rely on a baseline macroeconomic forecast, which incorporates projections of aggregate wages and employment. Because this baseline forecast does not allow for employment changes resulting from legislative options, no revenue effects are estimated for the proposed changes in the earnings test.

APPENDIX A

EFFECTS OF CHANGES IN THE SOCIAL SECURITY EARNINGS TEST, BY FAMILY INCOME, BY INCOME RELATIVE TO POVERTY THRESHOLDS, AND BY LIVING ARRANGEMENT, 1986

TABLE A-1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS, BY FAMILY INCOME AND EARNINGS (In percent)

Annual Family Income	Entire Group	With No Earnings	Earnings Under Limit	Earnings Over Limit
		Men		
Under $10,000	18	21	13	1
$10,000-14,999	16	18	19	2
$15,000-24,999	28	30	33	14
$25,000-31,999	11	11	11	12
$32,000-41,999	12	11	10	20
$42,000-49,999	4	4	3	9
$50,000-74,999	7	5	7	21
$75,000 and Over	4	1	3	23
All Incomes	100	100	100	100
		Women		
Under $10,000	26	28	21	a/
$10,000-14,999	17	16	21	10
$15,000-24,999	27	26	32	28
$25,000-31,999	11	11	10	14
$32,000-41,999	9	8	8	23
$42,000-49,999	3	3	3	4
$50,000-74,999	5	5	4	14
$75,000 and Over	2	2	1	8
All Incomes	100	100	100	100
		Men and Women		
Under $10,000	22	25	18	a/
$10,000-14,999	17	17	20	5
$15,000-24,999	28	28	32	19
$25,000-31,999	11	11	10	12
$32,000-41,999	10	9	9	21
$42,000-49,999	4	3	3	7
$50,000-74,999	6	5	6	18
$75,000 and Over	3	2	2	17
All Incomes	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Less than 0.5 percent.

TABLE A-2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS AND EARNINGS (In percent)

Family Income Relative to Poverty Thresholds	Entire Group	With No Earnings	Earnings Under Limit	Earnings Over Limit
		Men		
Under 1.0	7	9	5	1
1.0-1.49	11	13	9	a/
1.5-1.99	11	12	13	a/
2.0-2.99	24	26	25	6
3.0-3.99	16	15	20	12
4.0 and Over	31	25	28	81
All Ratios	100	100	100	100
		Women		
Under 1.0	11	12	6	a/
1.0-1.49	13	14	11	a/
1.5-1.99	12	12	14	1
2.0-2.99	23	23	27	16
3.0-3.99	16	15	19	23
4.0 and Over	26	25	22	60
All Ratios	100	100	100	100
		Men and Women		
Under 1.0	9	11	6	a/
1.0-1.49	12	13	10	a/
1.5-1.99	12	12	14	1
2.0-2.99	23	24	26	10
3.0-3.99	16	15	20	16
4.0 and Over	28	25	25	73
All Ratios	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Less than 0.5 percent.

TABLE A-3. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS, BY LIVING ARRANGEMENT AND EARNINGS (In percent)

Living Arrangement	Entire Group	With No Earnings	Earnings Under Limit	Earnings Over Limit
		Men		
Married Couples a/				
Living alone	61	61	56	65
With others	18	17	24	20
Widows/Widowers	8	9	7	5
Never Married	5	5	4	4
Separated/Divorced	8	8	8	6
All Arrangements	100	100	100	100
		Women		
Married Couples a/				
Living alone	48	50	35	41
With others	8	9	5	5
Widows/Widowers	31	30	43	32
Never Married	4	4	5	9
Separated/Divorced	8	8	12	14
All Arrangements	100	100	100	100
		Men and Women		
Married Couples				
Living alone	53	54	44	56
With others	12	12	14	14
Widows/Widowers	21	21	27	15
Never Married	5	5	4	6
Separated/Divorced	8	8	10	9
All Arrangements	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

TABLE A-4. NUMBER OF PEOPLE AGED 65-69 AFFECTED IN 1986 BY THE SOCIAL SECURITY EARNINGS TEST WHO WOULD NOT HAVE BEEN AFFECTED UNDER ALTERNATIVE EARNINGS LIMITS (In thousands)

Population Group	Earnings Limit Raised To: $9,000	$15,600	$22,560	Earnings Test Eliminated a/
Men	37	130	187	370
Women	48	138	188	223
Men and Women	85	267	374	594

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. This column is the same as the total number of people affected in 1986 by the earnings test.

TABLE A-5. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS AND THOSE WHO WOULD NOT HAVE BEEN AFFECTED UNDER ALTERNATIVE EARNINGS LIMITS, BY FAMILY INCOME (In percent)

Annual Family Income	Eligible for Benefits	Exempt from Earnings Test When Earnings Limit Raised To: $9,000	$15,600	$22,560	Earnings Test Eliminated
		Men			
Under $15,000	15	3	2	2	1
$15,000-24,999	12	7	13	13	9
$25,000-31,999	5	7	11	11	7
$32,000-41,999	5	21	14	12	13
$42,000-49,999	2	3	3	4	5
$50,000-74,999	3	4	6	7	13
$75,000 and Over	2	a/	a/	1	14
All Income Levels	43	44	49	50	62
		Women			
Under $15,000	24	15	9	6	4
$15,000-24,999	15	19	19	17	11
$25,000-31,999	6	a/	3	7	5
$32,000-41,999	5	13	11	9	9
$42,000-49,999	2	2	3	2	1
$50,000-74,999	3	4	4	6	5
$75,000 and Over	1	3	3	2	3
All Income Levels	57	56	51	50	38
		Men and Women			
Under $15,000	39	18	11	8	5
$15,000-24,999	28	26	32	30	19
$25,000-31,999	11	7	14	18	12
$32,000-41,999	10	34	25	22	21
$42,000-49,999	4	4	6	6	7
$50,000-74,999	6	8	10	13	18
$75,000 and Over	3	3	3	4	17
All Income Levels	100	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Less than 0.5 percent.

TABLE A-6. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS AND THOSE WHO WOULD NOT HAVE BEEN AFFECTED UNDER ALTERNATIVE EARNINGS LIMITS, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Family Income Relative to Poverty Thresholds	Eligible for Benefits	Exempt from Earnings Test When: Earnings Limit Raised To: $9,000	$15,600	$22,560	Earnings Test Eliminated
		Men			
Under 1.0	3	a/	a/	1	a/
1.0-1.99	10	a/	1	1	a/
2.0-2.99	10	5	6	6	4
3.0 3.99	7	9	12	11	7
4.0 and Over	13	30	30	32	51
All Income Levels	43	44	49	50	62
		Women			
Under 1.0	6	a/	a/	a/	a/
1.0-1.99	14	4	1	1	1
2.0-2.99	13	18	13	9	6
3.0-3.99	9	16	14	14	9
4.0 and Over	15	19	23	26	23
All Income Levels	57	56	51	50	38
		Men and Women			
Under 1.0	9	a/	a/	1	a/
1.0-1.99	24	4	2	1	1
2.0-2.99	23	23	19	15	10
3.0-3.99	16	24	26	25	16
4.0 and Over	28	48	53	58	73
All Income Levels	100	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Less than 0.5 percent.

TABLE A-7. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE TO RECEIVE SOCIAL SECURITY BENEFITS AND THOSE WHO WOULD NOT HAVE BEEN AFFECTED UNDER ALTERNATIVE EARNINGS LIMITS, BY LIVING ARRANGEMENT (In percent)

Living Arrangement	Eligible for Benefits	Exempt from Earnings Test When: Earnings Limit Raised To: $9,000	$15,600	$22,560	Earnings Test Eliminated
		Men			
Married Couples a/					
Living alone	26	25	28	28	40
With others	8	8	10	11	13
Widows/Widowers					
Living alone	2	4	1	2	1
With others	2	b/	2	1	2
Never Married	2	7	3	3	2
Separated/Divorced	3	1	4	5	4
All Families	43	44	49	50	62
		Women			
Married Couples a/					
Living alone	27	23	21	21	15
With others	5	b/	3	2	2
Widows/Widowers					
Living alone	13	12	12	11	8
With others	5	11	8	6	4
Never Married	2	4	2	4	3
Separated/Divorced	5	6	6	6	5
All Families	57	56	51	50	38
		Men and Women			**Men**
Married Couples					
Living alone	53	48	49	49	56
With others	12	8	13	13	14
Widows/Widowers					
Living alone	15	16	14	13	9
With others	7	11	9	7	6
Never Married	5	11	5	7	6
Separated/Divorced	8	7	10	11	9
All Families	100	100	100	100	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages and salaries, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

APPENDIX B

EFFECTS OF CHANGES IN THE SOCIAL SECURITY EARNINGS TEST, BY LIVING ARRANGEMENT AND INCOME RELATIVE TO POVERTY THRESHOLDS, 1986

TABLE B-1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY, BY LIVING ARRANGEMENT AND FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Living Arrangement	Family Income Relative to Poverty Thresholds					
	Under 1.0	1.0-1.99	2.0-2.99	3.0-3.99	4.0 and Over	All Income Levels
Men						
Married Couples a/						
Living alone	1	5	7	4	9	26
With others	1	2	2	1	2	8
Widows/Widowers						
Living alone	b/	1	b/	b/	b/	2
With others	b/	b/	b/	b/	b/	2
Never Married	b/	1	b/	b/	1	2
Separated/Divorced	1	1	1	b/	b/	3
All Families	3	10	10	7	13	43
Women						
Married Couples a/						
Living alone	1	5	7	5	9	27
With others	b/	1	1	1	2	5
Widows/Widowers						
Living alone	3	5	3	2	1	13
With others	1	1	1	1	1	5
Never Married	b/	1	b/	b/	1	2
Separated/Divorced	1	2	1	1	1	5
All Families	6	14	13	9	15	57
Men and Women						
Married Couples						
Living alone	2	10	13	9	19	53
With others	1	2	3	2	4	12
Widows/Widowers						
Living alone	3	5	3	2	2	15
With others	1	2	2	1	2	7
Never Married	b/	1	1	1	1	5
Separated/Divorced	2	3	1	1	1	8
All Families	9	24	23	16	28	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTE: Details may not add to totals because of rounding.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

TABLE B-2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 MADE EXEMPT FROM THE EARNINGS TEST BY RAISING THE EARNINGS LIMIT FROM $7,800 TO $9,000, BY LIVING ARRANGEMENT AND FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Living Arrangement	Family Income Relative to Poverty Thresholds					
	Under 1.0	1.0-1.99	2.0-2.99	3.0-3.99	4.0 and Over	All Income Levels
Men						
Married Couples a/						
Living alone	b/	b/	3	4	17	25
With others	b/	b/	b/	4	4	8
Widows/Widowers						
Living alone	b/	b/	b/	b/	3	4
With others	b/	b/	b/	b/	b/	b/
Never Married	b/	b/	1	b/	5	7
Separated/Divorced	b/	b/	1	b/	b/	1
All Families	b/	b/	5	9	30	44
Women						
Married Couples a/						
Living alone	b/	b/	3	6	14	23
With others	b/	b/	b/	b/	b/	b/
Widows/Widowers						
Living alone	b/	b/	7	5	b/	12
With others	b/	4	b/	4	3	11
Never Married	b/	b/	2	b/	1	4
Separated/Divorced	b/	b/	6	1	b/	6
All Families	b/	4	18	16	19	56
Men and Women						
Married Couples						
Living alone	b/	b/	6	10	31	48
With others	b/	b/	b/	4	4	8
Widows/Widowers						
Living alone	b/	b/	7	6	3	16
With others	b/	4	b/	4	3	11
Never Married	b/	b/	4	b/	7	11
Separated/Divorced	b/	b/	6	1	b/	7
All Families	b/	4	23	24	48	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

TABLE B-3. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 MADE EXEMPT FROM THE EARNINGS TEST BY RAISING THE EARNINGS LIMIT FROM $7,800 TO $15,600, BY LIVING ARRANGEMENT AND FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Living Arrangement	Family Income Relative to Poverty Thresholds: Under 1.0	1.0-1.99	2.0-2.99	3.0-3.99	4.0 and Over	All Income Levels
Men						
Married Couples a/						
Living alone	b/	b/	2	8	18	28
With others	b/	1	1	4	5	10
Widows/Widowers						
Living alone	b/	b/	b/	b/	1	1
With others	b/	b/	b/	b/	2	2
Never Married	b/	b/	1	b/	2	3
Separated/Divorced	b/	b/	1	b/	3	4
All Families	b/	1	6	12	30	49
Women						
Married Couples a/						
Living alone	b/	b/	3	4	14	21
With others	b/	b/	b/	b/	3	3
Widows/Widowers						
Living alone	b/	b/	5	6	1	12
With others	b/	1	1	1	4	8
Never Married	b/	b/	1	b/	1	2
Separated/Divorced	b/	b/	3	2	1	6
All Families	b/	1	13	14	23	51
Men and Women						
Married Couples						
Living alone	b/	b/	5	12	32	49
With others	b/	1	1	4	7	13
Widows/Widowers						
Living alone	b/	b/	5	6	2	14
With others	b/	1	1	1	6	9
Never Married	b/	b/	2	b/	3	5
Separated/Divorced	b/	b/	4	3	4	10
All Families	b/	2	19	26	53	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

TABLE B-4. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 MADE EXEMPT FROM THE EARNINGS TEST BY RAISING THE EARNINGS LIMIT FROM $7,800 TO $22,560, BY LIVING ARRANGEMENT AND FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Living Arrangement	Family Income Relative to Poverty Thresholds					
	Under 1.0	1.0-1.99	2.0-2.99	3.0-3.99	4.0 and Over	All Income Levels
Men						
Married Couples a/						
Living alone	b/	b/	3	7	18	28
With others	1	1	1	4	5	11
Widows/Widowers						
Living alone	b/	b/	b/	b/	1	2
With others	b/	b/	b/	b/	1	1
Never Married	b/	b/	1	b/	2	3
Separated/Divorced	b/	b/	1	b/	4	5
All Families	1	1	6	11	32	50
Women						
Married Couples a/						
Living alone	b/	b/	2	4	15	21
With others	b/	b/	b/	b/	2	2
Widows/Widowers						
Living alone	b/	b/	4	6	1	11
With others	b/	1	1	1	3	6
Never Married	b/	b/	1	b/	3	4
Separated/Divorced	b/	b/	2	2	2	6
All Families	b/	1	9	14	26	50
Men and Women						
Married Couples						
Living alone	b/	b/	5	11	33	49
With others	1	1	1	4	7	13
Widows/Widowers						
Living alone	b/	b/	4	6	3	13
With others	b/	1	1	1	5	7
Never Married	b/	b/	1	b/	5	7
Separated/Divorced	b/	b/	3	3	6	11
All Families	1	1	15	25	58	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

TABLE B-5. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 MADE EXEMPT BY ELIMINATING THE EARNINGS TEST, BY LIVING ARRANGEMENT AND FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS (In percent)

Living Arrangement	Family Income Relative to Poverty Thresholds					
	Under 1.0	1.0-1.99	2.0-2.99	3.0-3.99	4.0 and Over	All Income Levels
Men						
Married Couples a/						
Living alone	b/	b/	2	5	34	40
With others	b/	b/	1	2	9	13
Widows/Widowers						
Living alone	b/	b/	b/	b/	1	1
With others	b/	b/	b/	b/	2	2
Never Married	b/	b/	1	b/	2	2
Separated/Divorced	b/	b/	1	b/	3	4
All Families	b/	b/	4	7	51	62
Women						
Married Couples a/						
Living alone	b/	b/	1	3	11	15
With others	b/	b/	b/	b/	2	2
Widows/Widowers						
Living alone	b/	b/	2	4	2	8
With others	b/	1	1	1	3	4
Never Married	b/	b/	b/	b/	3	3
Separated/Divorced	b/	b/	1	1	2	5
All Families	b/	1	6	9	23	38
Men and Women						
Married Couples						
Living alone	b/	b/	3	8	45	56
With others	b/	b/	1	2	11	14
Widows/Widowers						
Living alone	b/	b/	2	4	3	9
With others	b/	1	1	1	4	6
Never Married	b/	b/	1	b/	5	6
Separated/Divorced	b/	b/	2	2	6	9
All Families	b/	1	10	16	73	100

SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

NOTES: Details may not add to totals because of rounding.
Income is distinct from earnings: earnings are wages, salaries, and income from self-employment, and are only part of total income.

a. Distributions of men and women in married couples are not the same because some married couples in the 65-69 age category have one spouse not between the ages of 65 and 69.

b. Less than 0.5 percent.

Chairman JACOBS. Was that a net figure calculating the additional taxes which might be paid by those who would in fact earn more?

Ms. GORDON. No, the table in the statement shows the amount of increased benefits that would be paid to Social Security beneficiaries. Estimates of the amount of revenues that would be collected if the change were made run around 10 to 15 percent of the amount of these benefits.

Chairman JACOBS. Mr. Daub.

Mr. DAUB. Thank you very much.

[Opening statement of Mr. Daub follows:]

The Honorable Hal Daub
Social Security Subcommittee Hearing
September 29, 1988

Chairman Jacobs, I want to thank you for agreeing to schedule this hearing on the social security retirement earnings test. While I do not view this as a necessarily partisan issue, I recognize that it is controversial. I appreciate your willingness to hear both sides of the issue presented.

Early in the 100th Congress, I introduced, H.R. 1555, a bill which over 5 years would phase out the retirement earnings test for workers over 65. The method I chose was to increase the threshold limits for four years in increments of $5000 each year. The test would be eliminated in the fifth year. The major appeal of this approach is that it benefits lower income workers first.

Subsequently, my colleague and former ranking Member of this Subcommittee Mr. Archer introduced H.R. 3794, a bill phasing out the retirement test by age for those now 65-69. That bill would be somewhat easier for the Social Security Administration to administer, since an increasing portion of beneficiaries would be freed from any restrictions each year.

I want to make it clear that I would support either approach as long as it would further the goal of removing this last vestige of age discrimination.

Mr. Chairman, I am very concerned with the implications of the CBO study on which this hearing focuses. Less than 600,000 of the 8 million people aged 65-69 who were surveyed elected to work in excess of the annual threshold amount. To put that another way, the retirement earnings test has helped to discourage 93% of eligible beneficiaries from working. Not surprisingly, many of those who elect to work in spite of the test have incomes that permit them to forgo benefits. The vast majority of middle-income beneficiaries, who are the most affected by the test, simply retire. A few, around 10%, work for less than the threshold amount.

I am not, of course, suggesting that all 93% would work full-time if the test were repealed. Clearly there are other factors involved. Still, as the demographics of the workplace reduce the number of workers entering the labor force, employers will turn more and more to our senior citizens. Those beneficiaries who have the motivation and health to work should not be discouraged from doing so by a marginal tax rate in excess of 50%! We need their contribution to the national economy.

While I understand the constraints under which CBO operates, it is unfortunate that CBO does not offset its cost projections by those contributions. Seniors who work contribute not only social security and income taxes, but also save the trust fund monies. Eliminating the retirement test would produce small administrative savings, and a major hassle for beneficiaries. Precisely estimating annual earnings is a challenge for many beneficaries. Under and overpayments are common.

I want to emphasize the fact that according to Social Security actuaries, repeal legislation has only short - range costs. In the long-term there are actually slight savings. This is because the "delayed retirement credit", which will increase benefits 8% a year for those who delay retirement after the turn of the century, washes out the long-term costs. Ultimately, the offsets I previously described result in net gains to the economy in general, and the trust funds in particular.

Mr. Chairman, I am not suggesting that repealing the retirement earnings test today will result in a great influx of seniors in the marketplace tomorrow. But, as we live longer and healthier lives, the option to return to work or continue to work will become increasingly more attractive as employers start

bidding for our talents and experience. It is to everyone's benefit, senior citizens, employers, and the national economy, to make that option viable. As the San Diego Tribune editorialized: "We think it is time that the law, not the older workers, be retired."

Mr. Chairman, I look forward to hearing from today's witnesses, and, again, I thank you for scheduling this important hearing.

Mr. DAUB. I want to commend you for giving this issue a hearing even at this late time in the Congress, because I suspect it can be a very productive area of work and for compromise in the upcoming session of the Congress.

I had a chance last night to read the testimony which you summarized. Can you tell me why the additional 1 million who worked for less than the exempt amount were not included in the CBO study?

Ms. GORDON. Well, those people——

Mr. DAUB. The study centered on the 600,000 and found many were not upper income?

Ms. GORDON. Right.

Mr. DAUB. There are another additional million workers that could have been affected by this particular formula, but they evidently weren't evaluated or analyzed?

Ms. GORDON. If those workers earn less than the $8,400 earnings limit, they aren't affected by the earnings test. They get to keep all of the earnings that they have and all of their Social Security benefits.

Mr. DAUB. But you didn't evaluate what kind of decisionmaking process they may have gone through to decide whether or not to keep on working?

Ms. GORDON. We have looked at the distribution of earnings of people who earn less than the exempt amount, and it is amazingly flat. If you consider how many people earn less than $1,000, between $1,000 and $2,000, between $2,000 and $3,000, and so forth, it is about the same number in each category up to the earnings test. In 1986, which was the date we were using, that amount was $7,800. There is then a dropoff in terms of the number of people who earn between $8,000 and $9,000, $9,000 and $10,000 and so on.

These findings suggest there may be some people who would in fact work more. But only 12 percent of those people who earn less than the limit were within $1,000 of the limit. I think if you were trying to control your earnings so as to remain around the limit, you would not keep them at half the limit; you would get closer. Only 12 percent of the people earning under the limit are within $1,000 of the limit and 22 percent are within $2,000 of it. It is really only that portion of the group, then, who might in fact change their behavior if the earnings test were raised.

Mr. DAUB. Did you take into account the 1982 and 1983 survey that the Social Security Administration conducted of 20 percent of those who were recent retirees? Did you take a look at that?

Ms. GORDON. We used the Current Population Survey for our study. To look at the total income these workers and their family had, you had to know of income from other sources the Social Security Administration data does not contain. We can't use SSA data to address these questions.

Mr. DAUB. What do you think might be the result if you did a careful evaluation of offsetting revenues from continuing work? Have you got some idea after you finished this report about what the impact of that might be?

Ms. GORDON. I think the estimates that have been done by, for example, the Social Security Administration [SSA], come out around 12 percent of the amount of the additional benefits. You

could take the numbers in table 1, for example, and calculate 88 percent of them, and that would give you a pretty good idea of the net cost of changing or eliminating the earnings test.

Mr. DAUB. But that would be a static analysis? Do you think it might have any effect on the behavioral activity of people in their choice of whether or not to work?

Ms. GORDON. That 12 percent includes the SSA's estimate of the additional taxes that you would get from the additional work effort of beneficiaries. If you just look at the additional taxes that you would collect on the benefits you would pay out, that they estimate that amount to be about 7 percent of the additional benefits.

Mr. DAUB. You may not want to offer an opinion on this, but the marginal tax rate certainly is overkill, isn't it? That is, it is in the range of 80 to 105 percent.

Ms. GORDON. That is certainly the case, if you reduce benefits by $1 for every $2 of earnings, during that period when earnings are going from the limit to the limit plus twice the PIA. In that range, you have to add 50 percent to what the marginal tax rate would otherwise be. But once earnings get above that, then, of course, the marginal tax rate drops back down.

Mr. DAUB. Of course.

Ms. GORDON. So people whose benefits are completely withheld are facing the same marginal tax rates as everybody else.

Mr. DAUB. What is the difference between whether you are lucky enough to be a higher income earner during your lifetime and then receive a penalty from what is supposed to be a rather neutral kind of a program, in which it is social security by an account number that doesn't know Francis Jones is a man or woman? We do decide when you get to be 65 if you are one of the most fortunate, that is you are more productive and have been more frugal and saved more or earned more or have worked harder all your life, and all of a sudden you find out that you are penalized to pay for someone else's benefit? Ultimately—at age 70—all that changes, and now it is OK for you to have all that money and all that extra money you paid in. Do you see this as any wise policy distinction as compared to 10 or 20 years ago?

Ms. GORDON. Certainly, in the case of people who continue to have high earnings, there is a reduction in their benefits through the earnings test, which is what you are referring to as a penalty. That doesn't apply if they happen to have high incomes from some other source, like interest on bonds or capital gains.

The other thing to bear in mind is that there is a delayed retirement credit, which partially offsets the impact of the earnings test.

Mr. DAUB. The one that will phase up to 8 percent over time?

Ms. GORDON. Yes. When it does reach 8 percent, it makes the earnings test actuarially fair. You get more later, and on average that should fully compensate for benefits lost because of the test. If, in fact, the people who continue to work after they are 65 are healthier on average than most beneficiaries, it would actually provide them with even more, because they would collect their benefits for a longer period of time than the life expectancy tables indicate.

Mr. DAUB. Of course, they are paying in taxes during that period of time too and adding to the solvency of the trust fund.

Ms. GORDON. Yes. But then again that may also raise their benefits.

Mr. DAUB. They are also going to raise the earnings limit three to one in 1990, right——

Ms. GORDON. I shouldn't interrupt, but we are going to cut the penalty.

Mr. DAUB. That is what I mean. Liberalize the penalty. They will be penalized less severely, one might argue, in 1990 because it will be a forfeiture of one for every three rather than one for every two?

Ms. GORDON. Right. You asked about the age break?

Mr. DAUB. Why age 70?

Ms. GORDON. My understanding is that initially there was not a limit. Then especially as more workers, such as farm workers, were covered, there was concern that in such occupations people may continue to work until they die. Therefore, such people would never be able to collect benefits. That is why an age limit was established. Over the years it has been gradually reduced to age 70.

Mr. DAUB. If we were going to use that logic, maybe we ought to have the earnings penalty in effect until 75 since we are living longer and are healthier. Maybe that is the direction we should be moving rather than the opposite direction.

Ms. GORDON. That is certainly a possibility. It depends on what your value judgments are, which, as you know, is your choice to make, not mine. But you have to decide whether you want to differentiate by the amount of earnings, by age, or by a combination of the two.

Mr. DAUB. I ought to introduce a bill like that. I think we would probably have more people in the hearing room today. I appreciate the careful work that you have done, and I believe additional work needs to be done by you with some parameters, perhaps, some exploring beyond just the static numbers. You work all your life to get the kids raised and out of the nest, I know what I am going through right now, I figure I will be 57 when the last one leaves home, although the door is always open, and they can come back. But in terms of college costs and all that, then you have just a few years if you are in middle America. You are looking at your retirement savings picture, and that changes rather dramatically as we look at the need for two-income families and two-income households now and the costs that are involved.

And I think with deregulated interest rates and the way in which other costs have changed, you have to worry about increasing your local tax base. If you have your house paid for by 60 or 65, you have that increasing property tax and just to keep the roof fixed creates other strains that maybe weren't there 10 or 20 years ago. Whether we repeal the earnings limitation or raise it will be the great debate, and the parameters for statistical analysis, I think, need to be perhaps directed toward you so we can get some additional analysis.

What you have given us so far is more appreciated. I, for one, appreciate the chance to have you here and ask you some questions.

Ms. GORDON. Thank you.

Chairman JACOBS. Ms. Wise.

Ms. WISE. Eliminating the retirement test has a very small long-range cost to the trust fund but a relatively large short-range cost. Can you tell us the impact of eliminating the retirement test on the ability of the Social Security Trust Fund to pay benefits in the future?

Ms. GORDON. That gets into an area where different viewpoints are held by different people. I think everyone agrees on one point: if you spend more money for Social Security or anything else, that increases the shortfall that we have between the revenues we are collecting and the total spending that is being done by the Federal Government. That means the Treasury has to borrow more in private credit markets now, and that may lead to less private investment.

Many economists are concerned that high Federal borrowing reduces private investment, which would in turn reduce the output we would have in the future and make it harder to support the much larger elderly population that we will have in the next century.

The other impact concerns the Balanced Budget Act, which establishes targets for the Federal deficit. Although Social Security is now off the budget, it is counted for purposes of meeting these deficit targets. Therefore, if more were spent through the Social Security program, there would have to be either greater reductions in other spending programs or more tax increases in order to meet those targets.

Ms. WISE. Thank you.

Chairman JACOBS. Ms. Gordon and your colleagues, we thank you for your contribution to the record.

Ms. GORDON. You are very welcome.

Chairman JACOBS. Our next witness is one of the smartest, wisest, most intellectually honest Members of the U.S. House of Representatives, Bill Archer, who is entitled to be mistaken now and then. If you would yield to Hal.

Mr. DAUB. I do want to thank you for agreeing to schedule this hearing on the Social Security retirement earnings test. I do not view this as a necessarily partisan issue, but I recognize that it is controversial. I appreciate your willingness to hear both sides of the issue presented.

Early in the 100th Congress, I introduced H.R. 1555, a bill which over 5 years would phase out the retirement earnings test for workers over age 65. The method I chose was to increase the threshold limit for 4 years in increments of $5,000 each year, ultimately abolishing it in the 5th year. The major appeal of this approach is that it benefits lower income workers first.

Subsequently, my colleague and former ranking member of this subcommittee, now the ranking member of the full committee, who is about to testify, Mr. Archer of Texas, introduced H.R. 3794, a bill phasing out the retirement test by age for those now 65 to 69. That bill would be somewhat easier for the Social Security Administration to administer since an increasing portion of beneficiaries would be freed from any restrictions each year.

I want to make it clear I would support either approach as long as it would further the goal of removing this last vestige of age discrimination.

Mr. Chairman, I am very concerned with the implications of the CBO study on which this hearing focuses. Less than 600,000 of the 8 million people aged 65 to 69 who were surveyed elected to work in excess of the annual threshold amount. To put that another way, the retirement earnings test has helped to discourage 93 percent of eligible beneficiaries from working. Not surprisingly, many of those who elect to work in spite of the test have incomes that permit them to forgo benefits. The vast majority of middle-income beneficiaries who are the most affected by the test simply retire, a few, around 10 percent, work for less than the threshold amount.

I am not, of course, suggesting that all 93 percent would work full time if the test were repealed. Clearly there are other factors involved. Still as the demographics of the work place reduce the number of workers entering the labor force, employers will turn more and more to our senior citizens. Those beneficiaries who have the motivation and health to work should not be discouraged from doing so by a marginal tax rate in excess of 50 percent. We need their contribution to our national economy.

While I understand the constraints under which CBO operates, it is unfortunate that CBO does not offset its cost projections by those contributions. Seniors who work contribute not only Social Security and income taxes but also save the trust fund money. Eliminating the retirement test would produce small administrative savings and a major hassle for beneficiaries. Precisely estimating annual earnings is a challenge for many beneficiaries; under and overpayments are common.

I want to emphasize the fact, according to the Social Security actuaries, repeal legislation has only short-range costs; in long-range terms there are actual slight savings. This is because the "delayed retirement credit", which would increase benefits eight percent a year for those who delay retirement after the turn of the century washes out the long-term costs. Ultimately, the offsets I previously described result in net gains to the economy in general and the trust fund in particular.

Mr. Chairman, I am not suggesting that repealing the retirement earnings test today will result in a great influx of seniors into the marketplace tomorrow, but as we live longer and healthier lives, the option to return to work or continue to work will become increasingly more attractive as employers start bidding for our talents and expertise. It is to everyone's benefit, senior citizens, employers and the national economy, to make that option available.

As the San Diego Tribune editorialized, and I quote them, "We think it is time that the law, not the older workers, retired." Mr. Chairman, I look forward to our colleagues, particularly to the man you well introduced who I think is the most, if not one of the most, knowledgeable Members of the Congress when it comes to Social Security matters, and we look forward to his testimony.

STATEMENT OF HON. BILL ARCHER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. ARCHER. Thank you very much.

At the outset, I would say that I am in total agreement with the entire statement of our colleague from Nebraska, Mr. Daub, and to

further say that this subcommittee and the full committee and the Congress will miss him next year, miss his intellect, his ability to turn a phrase, and I wish him well.

I do particularly appreciate your scheduling this hearing in the waning moments of this Congress, Mr. Chairman.

Chairman JACOBS. I might say to my colleague, this is Hal's going away present.

Mr. ARCHER. It is well earned. Now all we have to do is put something in the box, only the wrappings are there for the present.

I am particularly delighted to be able to speak on this subject. Although you and I have some disagreement, which is unusual in the area of Social Security, as the chairman knows, I was the first to introduce legislation to repeal the earnings limitation, and I have reintroduced it in one form or another ever since I have been in the Congress. It might be of interest to the members of the committee to know that the Senate sponsor over all those years, until his retirement, was Senator Barry Goldwater, and I think it would be a marvelous present for him as a retired elderly statesman to be able to see the fruition of his efforts over the years. In my opinion, the earnings limit is an anachronism left over from the depression. When Social Security was first enacted in 1935 the earnings limit was put in for two immediate aims, as I read history: to provide benefits to replace earnings lost through retirement, and to offer an incentive for older workers to make way for younger workers who wanted to enter the work force.

And at that time there were far more workers than there were jobs. But the changing demographics of the work place have completely overtaken those depression era goals.

During World War II, we had 50 workers for every Social Security beneficiary. Today there are just over three. And the projections are, as all of you on the committee know, that in another 50 years that will be reduced to two workers for every beneficiary. According to newly released statistics from the Department of Labor, the median age of workers is climbing. By 1989, there will be 15 million fewer people age 18 to 25 than today.

The sharp decrease in entry level employees means older workers are going to be needed to fill employment gaps, the complete reversal of what we had back during the Depression years when social security was put on the books. More importantly, our economy needs the skills and experience of senior workers. I agree with former Secretary of Labor, Bill Brock, who said we ought to establish a new ethic in this country, that everybody ought to have the right to work as long as they want and are capable of working.

Senior Americans are increasingly more skilled, consistently more reliable, healthier than ever and desperately needed to fill a growing employment vacuum. It is an affront to those people that the earnings limit remains a strong disincentive, as you said, Hal, for Social Security beneficiaries who want to continue to contribute to society through their productive efforts and to improve their own financial situation.

The earnings limitation is most onerous in its effect on middle-income workers between 65 and 69. As has been mentioned, it takes away $1 for every $2 of benefits, and it effectively imposes a high marginal tax rate of 50 percent on all income earned over

$8,400. When income and payroll taxes are calculated, the marginal rate can be actually much higher than 50 percent. We still hear the biggest reason not to repeal the limit is because it would benefit upper income workers. The fact of the matter is only upper income beneficiaries can afford to work in spite of the current limitation.

In my review, they would not be the group most affected by a repeal, and I believe that later this morning Commissioner Dorcas Hardy will have something to say about that relative to the CBO study.

The upper income workers benefit most by the delayed retirement credit, and by deferring benefits until retirement, which may put them in a lower tax bracket. And, interestingly enough, we have a situation, as testified to by the CBO which is what we called in tax reform of 1986 the "bubble effect." The proponents of tax reform said we are going to have a maximum tax rate of 28 percent, but then they said once you get over a certain amount of taxable income, you lose the benefit of the 15 percent on your earlier income, and you have to phase out the benefits of your dependency, and as a result, single taxpayers who are earning over $41,000 a year end up having to pay a 33-percent real rate until they have phased out the so-called benefits.

So they pay that until they reach a certain taxable dollar figure that is over $100,000, and then when they get beyond that and they get into really upper income tax brackets, they go back to 28 percent. Weird.

And you have got a similar situation as a result of the retirement test. Once you get to a very high income, you phased out all your Social Security benefits, and then you go back to a true effective tax rate that is much, much below the 50 percent. Fascinating, Mr. Chairman. In fact, I didn't really appreciate that until I heard the CBO testimony this morning.

It's clear that the group which are most hurt are lower and middle income workers. A special 1982 survey conducted by the Social Security Administration underscored that fact. The occupations of those surveyed who continued to work after they received their first benefit check were located in the vast marketplace of the middle-income jobs: sales, transportation, farming, precision production, crafts and repair.

Moreover, the survey showed that working beneficiaries did not continue to work the same hours and, more importantly, did not continue to receive the same pay. For example, the average male beneficiary who continued to work after his retirement worked about one-half time for one quarter of his preretirement pay.

Although the typical beneficiary did not change professions, he experienced a dramatic drop in median hourly wage. Male beneficiaries had a median hourly wage of $5.12, women $4.29. The sharp drop in median hourly wage, without shifts in occupations, leads one to the undeniable conclusion that the earnings limit serves as a subtle form of wage discrimination against older Americans.

As a matter of equity and fairness, I strongly favor outright, across-the-board repeal of the earnings limitation. Estimates of initial short range revenue costs, however, make such legislation difficult to advance in this age of necessary deficit reduction. The good

news is that Social Security actuaries assure me that there are no long-term costs, and you have already heard that from the CBO testimony today, all major revenue losses occur in the early years.

In an effort to minimize the initial costs, I have introduced H.R. 3794, the Worker's Option Act of 1988. This bill would phase out the limit starting with those over age 69 in the first year, over age 68 in the second year, and so on until it is totally phased out in 5 years. Even that costs a good bit of money to the fund. The CBO estimates are over $7 billion over a 5-year period. However, they do not take into effect, as you mentioned, the offsets for the additional payroll taxes that will come into the fund by virtue of people working and, of course, they do not in any way take into account the behavorial patterns and the resulting increase in revenues to the general treasury as a result of people being out there working productively and paying more income tax.

So we really do not have adequate data as to what the net cost would be. But certainly if benefits—Mr. Chairman, you and I have heard this from all our colleagues over the years—if benefits under Social Security are an earned right, and I don't hear any Members of Congress telling people they are not an earned right, then when people reach the age of retirement, full retirement at age 65, if they have earned it they should receive it regardless of what they do thereafter. Unless we repeal the earning limitation as a matter of equity, we still have inequity in the Social Security Act, and we cannot legitimately go to those who have worked all their lives and reached age 65 and say you have an earned right.

The entire legislation offered may not be enacted and I understand the problems. I would be happy to see us move in the direction of the ultimate goal step by step in whatever way the subcommittee believes is desirable, whatever formulation, whether it is increasing the cap, whether it is phasing it in by age over a longer period of time, whatever method we take to move that up, the nation will benefit.

I want to thank today's witnesses and I want to tell the committee that I am sorry former Chief Actuary Bob Myers could not be with us today.

He wanted to be, but he has submitted detailed testimony in favor of repeal and I am sure the subcommittee has that.

Finally, I want to acknowledge, if I may, with your indulgence, Mr. Chairman, this is proceeding a little bit out of order, but I would like to acknowledge, the contributions that Arthur Pete Singleton, minority chief of staff of the Ways and Means Committee has made to this subcommittee over all of its years of existence. He is well-known to his friends for these contributions. He is retiring next week and this is the final Social Security hearing on his watch.

I must say he was my tutor when I first went on the Ways and Means Committee when we had no Subcommittee on Social Security and no individual Member was really interested in getting into it, and he tutored me and encouraged me to get interested in Social Security; and were it not for him, I would not have the knowledge that I have today.

He has been a good friend of the Social Security program and is emotionally involved in it, and I want to salute him and wish him well in the years ahead.

Chairman JACOBS. I think we should let the record show Mr. Singleton is suitably and modestly red-faced.

Mr. ARCHER. Thank you, very much, Mr. Chairman. If there are any questions, I would be glad to try to respond.

Mr. DAUB. I certainly appreciate the fact that you will be here next year in an even more important capacity as the ranking member of the full committee. This legislation will, indeed, have an opportunity to be explored and somewhere between repeal I think will be the fair goal, as you just said, and the budget considerations of the early outlays, some compromise as we move to that goal would be the result or could be the result.

So thank you for your leadership on Social Security issues, but most especially this issue, the subject of the hearing today. I couldn't agree more with the statement which will now be an important part of the record.

Mr. ARCHER. Thank you, very much.

Chairman JACOBS. Mr. Gibbons.

Mr. GIBBONS. I want to say it was excellent testimony, and I want to say to Pete Singleton, we are going to miss you, Pete. You have made a great contribution to the country's welfare.

I have a little personal conflict of interest with the retirement test, but nevertheless I think you are right.

Chairman JACOBS. Bill, I would like to make a couple of comments and point out some other possibilities.

One, Hal said that some people, because they work harder, have some money and so on, I am not so sure that is what the statistics show exactly, they are the people who necessarily work harder. Usually the people who can command high personal incomes into their senior years are professional people, lawyers, doctors, people like that.

I practiced law before I came to Congress; I also dug ditches before I practiced law, and as between the two, I think I worked a little harder when I dug the ditches. That is the reason why I think the Congress opposed rather vigorously the administration's suggestion that early retirement be essentially eliminated back in 1981 or 1982 when that proposal was made to reduce the early retirement benefit from 80 percent to 55 percent, as I recall, because the fellow who had dug ditches or the woman who scrubbed floors was pretty worn out by the time he or she got to be 62, so I am not sure it turns necessarily on who works harder, maybe who is born into the right family to have the right kind of background for their education. Others with fewer opportunities in the beginning managed to break through and acquire professions, but at least that is a factor.

Also, I hear it said there should be a right to work, and I couldn't agree more. I am not sure there is a right to work and pretend you are not working, but retired. That seems to be the nub of the issue. As far as the concept of a taxation because of the penalty foregoing beyond the retirement test, I would suggest there is an important distinction between that penalty and taxes.

In the case of taxes, you pay. In the case of a penalty, you pay back what has been given you in retirement benefits when it is determined in fact, according to the law, you have not been retired.

Finally I suggest for our consideration, the right that is earned in any contract is governed by the terms of the contract, and while the American public was earning the right, its rights under Social Security, old age and survivors, it was earning the right to retirement benefits. It seems to me since that was the condition all the time the American people have been paying in, we have earned the right according to the contract terms itself which include the retirement test.

So whether there is wisdom or there is not in repealing the retirement test or relaxing it or increasing the amount, it seems to me that it might be more reasonable to say that the rights which have been earned by paying into the system are the rights which were described in the system into which we have paid. Now, tear that up.

Mr. ARCHER. Mr. Chairman, I would be pleased to enter into friendly discussion with you about that. I am not sure that with the other witnesses waiting to testify this is the appropriate place, but I know your views and I know they are genuine and sincere and I guess you can take any set of figures you want and make different interpretations.

But I do thank you for giving me the opportunity to present this testimony.

Chairman JACOBS. I think both of us just don't want to get the notion we agree on everything.

Mr. ARCHER. That is right. Thank you, Mr. Chairman.

Chairman JACOBS. Thank you.

Our next witness is our colleague, Ben Gilman.

STATEMENT OF HON. BENJAMIN A. GILMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. GILMAN. Thank you, Mr. Chairman, members of the committee. I want to take this opportunity to commend you for conducting this hearing. Attention to this issue is long overdue. It is kind of an anachronism that we have these limitations on earnings and I hope we can find some solution to it as a result of your hearings. I welcome the opportunity to express my support for removing the constraints on our senior citizens' ability to remain productive and self sufficient throughout their retirement years.

For the past several sessions of Congress I have had the opportunity of introducing legislation which would increase the Social Security earnings' limitation to a level in keeping with some of our current economic conditions. The measure I introduced, H.R. 351 would allow beneficiaries to earn outside income of $8106 between the ages of 62 and 64 and $10,920 between the ages of 65 and 69. That measure would allow our nations' seniors to retain their productive capacity and at the same time maintain the self esteem of employment without suffering benefit reductions and without placing an undue hardship on our Social Security system.

I would much prefer to see us eliminate the entire earning limitation, but if we have to find some reasonable area of compromise, I suggest you might want to look at the formula I have suggested.

The recently published Congressional Budget Office [CBO] report estimates that raising the earnings limitation to $10,000 in 1989 would increase outlays by about $1.3 billion over the 1989–1993 period. According to CBO, complete elimination would cost nearly $24 billion over the same 5 years. I believe these figures to be somewhat overstated.

The CBO analysis ignores the fact that costs incurred from outright elimination would be partially offset by the recoupment of revenues resulting from the substantial amount of the workforce put back on the employment rolls. As we all know, there is a significant amount of so-called underground income that is not reported by our senior citizens as a result of this overly burdensome limitation placed on them. In other words, seniors who want to earn additional income, without suffering a reduction in their Social Security benefits, are earning a substantial amount of money and not reporting it. The limitations test presents seniors with a disincentive to do what is proper and with a simultaneous disincentive to retain their productive capacities.

The increase, or outright repeal, of the retirement earnings limitation would also increase the fairness of Social Security by treating earned income in the same way as unearned income. We are all aware of the fact that there is no reduction from Social Security benefits for investment income, stock dividends, and interest, beyond the age of 65. The inequity in this system is apparent, and it is time that we made certain that those who want to work honestly above the board can enjoy the same benefits as those who choose to retire and take their subsistence solely through Social Security income.

We are all too familiar with the heavy financial burden already borne by senior citizens. This, coupled with the depression and loneliness which often accompany the later years in one's life, speaks for the need to encourage older Americans to continue being productive, enterprising members of our community. In conclusion, I hope that the Committee on Ways and Means will move swiftly to reform or modify the Social Security earnings test, which I noted earlier I think is an anachronism in this day and age.

I thank you, Mr. Chairman.

Chairman JACOBS. Mr. Daub.

Mr. DAUB. I have no questions except to commend you. Your bill is going to add to the debate which I hope will occur next year to a positive result. We have cosponsors now and your leadership is going to be needed to bring about a solution to this problem.

Mr. GILMAN. I thank the gentleman. I know of his continuing interest in this area.

Mr. GIBBONS. Well done.

Mr. GILMAN. Thank you, gentlemen and Mr. Chairman for your time.

Chairman JACOBS. Our next witness is Mr. Bilirakis.

STATEMENT OF HON. MICHAEL BILIRAKIS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. BILIRAKIS. Thank you.

Mr. GIBBONS. Our neighbor and friend. He represents people right next door to us. A very fine Member of Congress.

Mr. BILIRAKIS. I want to say, Mr. Chairman, that I thank you and commend you for holding today's hearing. Mr. Chairman, much of it has already been said and will, of course, be said by those following me and I don't know how much more I can add, but I will try at least to share with you and this fine committee the feelings, if you will, of coming from probably the most elderly area of the country. Mr. Gibbons can certainly identify with that.

I feel very strongly about this subject and have for quite a long period of time. I thank the committee for giving me an opportunity to be heard this morning.

Mr. Chairman, my Florida district, as I have already said, consists of one of the highest concentrations, I think the highest or certainly no less than the second highest concentration, of senior citizens in the country. Ever since I was first elected to represent them, I have heard discord from many of them about the issue before us today.

The message which I hear from my constituents on this subject is a clear one. They tell me emphatically that they feel the earnings limitation which is imposed upon them is unfair. Quite frankly, and obviously, I agree with them and that is why I have cosponsored Mr. Archer's legislation which he explained to the committee earlier. It is my feeling that the current Social Security limitation earning, which penalize capable individuals who are able and willing to work and after all that should be the American way and always has been the American way, that should be repealed and repealed soon.

The current loss of $1 for every $2 earned above the threshold is bad policy. We should be encouraging these individuals to continue to be productive contributing members of our society.

They have an awful lot to add, Mr. Chairman, and the way it is now, we are really discouraging them from contributing. Instead of encouraging them, we are discouraging them by taking away some of their benefits for continuing to work.

I commend Social Security Administrator, Dorcas Hardy, for going on record as supporting liberalization of the Social Security earnings limitations before the current target date of 1993. The reality is that the current policy must be changed before 1993, it must be changed now.

The reality is that the senior citizens of our society are living longer, healthier lives and when we established these rights, Mr. Chairman, and these rules, goodness knows the age span was a great deal less. As a result they will be able to continue to work and contribute to our society through their wisdom, through their expertise, not to mention their payroll taxes, for longer periods of time.

In addition, physical reality necessarily requires today's senior citizens to supplement, and this is something we see in my area, their Social Security benefits with additional income from employ-

ment as long as they possibly can. They should not be penalized for doing this, Mr. Chairman.

The Social Security benefits are something that they have already worked for and something they have earned. An individual's guarantee of Social Security benefits after completion of a specified number of working quarters should be a given. We have told them this all through the years.

Whether or not they want and are able to continue working past the traditional retirement age should not be a factor in determining how much of their Social Security benefits they will receive. They have already earned, based on formulas created by the Congress, and they are entitled to, their full Social Security retirement benefits.

Mr. Chairman, I come from a family of Greek immigrants who literally live to work. In this sense, I know many individuals who, I think quite honestly would wither away and die if they had to stop working. I am certain you too, Mr. Chairman, know many people like this. Work for these individuals is their way of feeling that they are productive, contributing members to society. Once such people are forced to stop working, they often withdraw into sickness and depression which is often irreversible.

My point, Mr. Chairman, is that we cannot set a magic age at which we mandate that people should retire. Everyone is different with different capabilities. The age at which one individual chooses to be able to work may be 10 years away from another individual's age at which he should stop working. The important point is that both these individuals have earned their Social Security benefits again based on rules that we, the Congress, have established and are entitled to them.

For these reasons, Mr. Chairman, I would like to encourage you and your distinguished subcommittee to put yourselves in the shoes of the senior citizens of our district on this issue. Think about how you would feel if, after a lifetime's work and contribution into the Social Security trust funds, you had a portion held back because you continued to work past the age which the bureaucracy has deemed appropriate for retirement.

I hope you will all see the injustice in this current policy and act quickly to reverse it. The senior citizens and future senior citizens of our country are sure to thank you.

Thank you for the opportunity to be heard.

Mr. GIBBONS. A very fine statement. I agree with you 100 percent.

Mr. DAUB. You always have been the leader. I know we got acquainted when you first started serving on the Aging Committee. Your work is going to be needed next year to bring this to a successful result.

Mr. BILIRAKIS. Thank you. I wish you were going to be here working with us on this subject.

Chairman JACOBS. Mr. Wyden, from the great northwest.

STATEMENT OF HON. RON WYDEN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OREGON

Mr. WYDEN. Thank you, very much, Mr. Chairman. I will be very brief. I know we have a vote.

Let me throw the bouquets to Hal Daub and Pete Singleton as well for a great job. I have introduced the Elderly Earnings Act of 1987, H.R. 620; what that would do is raise the amount older people could earn over a 10-year period to the average salary in this country. If you were to estimate it today Social Security has determined it to be in the vicinity of $18,000.

I want to make it very clear who I am concerned about, Mr. Chairman, because I think there has been an awful lot of rhetoric on all sides of this issue. I want to make it clear who I think the important people are. I am concerned about the divorced woman who, I think, is going to be coming back to the work force in disproportionate numbers in the years ahead.

It is an older individual who doesn't have a long track record of work, who doesn't have a lot already in the earnings file, somebody who probably hasn't had access to a wide range of training programs and the like, somebody who, I think, is really hurt by the current limitation.

The kind of person I am concerned about would be the older worker—someone who did hard physical labor during the first part of their working life, became physically exhausted and had to go back into the work force and was looking for positions like secretary, department store worker, a working social services program, stay with kids, those are the kinds of people I am concerned about.

They are not people who can clip coupons. I would like to say it right at the outset, people like Malcom Forbes, and Lee Iacocca are people with tremendous talents who can make it in the marketplace. They are not the centerpiece of what this issue is about. The centerpiece are those low and moderate income people who, I think, are really particularly with today's skyrocketing medical bills being pushed into a position where they can't pay for necessities because of the earnings limit.

I thought that one statistic really summed it up for me very well, Mr. Chairman. The poverty rate in 1987 for an elderly single individual was $5,500. So if you use the 1987 figure without additional income, seniors receiving an average Social Security check are kept close to the poverty level by the earnings test.

So when I take into consideration in my legislation is that group of people as the target group and try to raise the amount that they can earn over a 10-year period. The actuaries for the system gave us a memo and I would like to make it part of the record, that says that is probably a way that we can hold the cost down. For example, in calendar year 1990, the first year that my approach would go into effect, they estimate the cost of the additional benefit period would be $1.3 billion. It is still an awful lot of money in anyone's calculation, but a way to address the concern of the low and moderate income older worker, particularly those kinds of people in a way that is less costly to the system than a variety of other approaches.

The other thing I think is particularly important that we do, Mr. Chairman, is to equalize the situation for workers between the age of 62 and 64 to the benefit levels of those that are between 65 and 69. The Social Security Administration says that those are the neediest people, their repeated studies have shown.

So the first part of my bill equalizes the treatment of those between 62 and 64 and those between 65 and 69 and then it raises the earnings ceiling $1,000 a year in effect over a 10-year period.

I think I am going to break the speech off right there, Mr. Chairman. You have been awfully kind to me in the times we have talked about it and I want you to know finally that I am very much aware and wish to be sensitive to your point about who is going to be helped here and I think that there is a significant block of older people in a volatile rapidly changing economy that are going to come back to these positions, largely service oriented positions. They will be making very modest incomes and their medical bills alone are going up faster than anything that has happened on the social security side. That is why I would like to see them be in a position to earn a little more.

Chairman JACOBS. Mr. Daub.

Mr. DAUB. Just that the taxicab driver or refuse hauler or computer programmer are all going to be affected. These are people in my judgment being penalized when they want to continue being productive for whatever reason. They need to pay bills or just want to work. I couldn't agree with you more. I appreciate your leadership.

Chairman JACOBS. I assume if these people will earn modest incomes, a modest increase in the test will do.

Mr. WYDEN. Yes. That is what I seek to do in the bill.

[The prepared statement follows:]

STATEMENT OF
THE HONORABLE RON WYDEN
HEARING ON THE SOCIAL SECURITY EARNINGS TEST
BEFORE THE
HOUSE WAYS AND MEANS
SUBCOMMITTEE ON SOCIAL SECURITY
SEPTEMBER 29, 1988

Mr. Chairman, I appreciate you providing this opportunity to discuss my proposal on the Social Security Earnings Test. There are many low and moderate income elderly who are unfairly discriminated against under the earnings test.

I introduced legislation at the beginning of this Congress to get rid of these iniquities. H.R. 620, the Elderly Earnings Opportunity Act of 1987, will reduce but not eliminate the penalties our older citizens face when they choose to work.

My greatest concern has been that there are low and moderate income elderly people, lacking stocks, bonds and mutual funds that are presently expected to supplement their incomes and live in today's economy where the elderly's medical costs are gobbling up every dollar they have.

My proposal addresses these concerns in three ways: First, it lifts the earnings limit for working retirees 62-64 to the same level as for those 65-69. For those who are 62-64, the cap is $6,120 and for those who are 65-69 the cap is $8,400 this year. In contrast, the poverty level for elderly, single individuals is $5,500.

Second, it gradually phases in an increased earnings cap to meet the average wage of workers -- presently about $18 - $19 thousand a year. Finally, it requires the Social Security Administration to report to Congress on the effect of the earnings test on the well being of the elderly and the economy in general.

H.R. 620 targets its relief on those who need it the most -- those just under 65. Social Security studies have repeatedly shown that these retirees are the needier beneficiaries. In addition, my bill would make more fair the treatment of workers between 65 and 69 by giving them the opportunity to contribute in the economy.

These are more likely to have been in arduous occupations, more likely to have done blue-collar work, more likely to be suffering from work-limiting health conditions and more likely to have lower benefit levels.

But many of them can do other less demanding jobs than they did in their earlier years -- and probably would if it weren't for the earnings test. Perhaps they would choose to take a position in a department store or work with kids -- all jobs that allow active people a chance to contribute to their own welfare and to society as a whole.

I do recognize that my bill carries some costs. The Social Security Actuary estimate is $ 10.2 billion over 5 years. However, the Actuary has also estimated that 20% will be generated back into the economy. My approach both recognizes today's fiscal limitations and our need to eliminate an unfair barrier.

First, the changes are put off until 1990. Second, I have only made moderate increases in the earnings allowance. Finally, I have targeted my bill only to those low to moderate income beneficiaries that most need the help.

Mr. Chairman, the earnings test was devised in a different time and under different economic conditions than we face today. In the 1930s, during the Great Depression, this country was looking for innovative solutions to a stagnant economy and catastrophic losses to individuals. The social security system was an ingenious way of solving all those problems.

Things have changed. Today's economy needs older workers. It needs their individual service, their production and the cumulative experiences they bring to the workforce -- skills, talents, and good judgment.

We must reduce the major hidden tax that keeps our seniors of moderate means from working. Those lacking substantial unearned income should be given greater opportunity to improve their own well being while contributing to society to the best of their ability.

Chairman JACOBS. Let's go vote. Ms. Hardy, we will get back as quickly as we can. We apologize, we know you are busy.

The subcommittee will resume its sitting.

Our next witness is the Commissioner of the Social Security Administration, Ms. Dorcas Hardy. As always, we are pleased to have your participation and contribution to the record.

STATEMENT OF HON. DORCAS R. HARDY, COMMISSIONER OF SOCIAL SECURITY, U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Ms. HARDY. Thank you, Mr. Chairman. It is a pleasure to be here.

I want to first thank you for scheduling this hearing, because I think the issue, as we have talked, deserves considerable public discussion. I am also pleased so many Congressmen have already shown their support for the elimination of the retirement earnings test. I especially commend Representative Archer and Representative Daub for their leadership in this area.

I have formal remarks. I will summarize them for you. I am not quite sure who had the bright idea of calling the retirement earnings provision a test, because the only thing that it appears to test is the mettle of the beneficiaries who try to live with it, and also the patience of the Social Security Administration employees who try to administer it.

I don't think it is a test. I do believe it is a penalty. Many older Americans who want to continue working and who want to be active and productive members of society are being penalized by our government for no particular reason other than, in addition to working, they happen to be over 65, and they happen to be eligible for Social Security. Whatever reasons that legislators had for establishing the law in the first place—and I think some colleagues have already discussed that—they are no longer practicable or pertinent.

I believe the retirement earnings penalty is antiquated and it should be eliminated. The penalty limits older workers' freedom to work and to improve their financial security. It causes Social Security Administration to spend scarce administrative resources on enforcement activities. There are ways to deal with the cost of eliminating the penalty.

We know how it works. That has been reviewed this morning. But each year more than 700,000 Americans age 65 to 69 lose some or all of their benefits due to the law. Many other persons in this age group deliberately limit their reported earnings to the exempt amount so they will not lose benefits, and many others don't report at all.

Workers who are eligible for Social Security benefits at normal retirement age should be able to decide whether they want to work and how much they want to work without having to worry about losing their benefits. People, we all know, are living longer. They are healthier, fortunately, than when Social Security began 50 years ago. I do not believe the Government should be the one encouraging them to sit out those years if they are willing and able to work.

The current law discriminates against low and middle-income workers, as Congressman Wyden pointed out, because it applies only to earned income, not to investment income that many well-to-do retirees count on to supplement their Social Security. Thus, the factory worker or the dishwasher who cannot afford to fully retire at age 65 pays a harsh penalty while the business executive or the physician, who was financially able to invest in stocks or bonds or annuities, may retire with all that investment income and their full benefits as well.

The earnings penalty is also extremely unpopular with the public. As is often true with unpopular laws, it has unfortunately encouraged otherwise law abiding senior citizens, especially those who need additional income, to circumvent the law by joining the "gray underground economy." Although this is regrettable, it is also perhaps understandable. Not only do they not have the earnings penalty, they also pay no FICA. They pay no income taxes, either.

So the penalty adversely affects our national economy in several other ways. It encourages older workers to leave the work force and it has, I think, diminished the supply of educated and trained and experienced labor, and we all know we will need even more of that in the not too distant future.

The Congress has already taken us a long way toward ending discrimination against older workers by eliminating mandatory retirement, prohibiting employment discrimination based on age, and enacting numerous other measures designed to allow seniors to continue healthy and productive lives.

Elimination of the retirement earnings penalty would clearly be another major step in this direction and should be enacted. It would be consistent with the other kinds of views that have preceded legislation in these areas.

Earlier I also mentioned the burden of administering the current law. We do spend considerable resources not only explaining and enforcing the penalty, but also in recovering the overpayments that are an inevitable result of the very complex rules and the reporting requirements.

I spend a lot of time visiting many of our field offices throughout the country and there are several horror stories that you hear. The frequent one seems to be one that was told to me by an employee in an Idaho district office whose mother receives retirement benefits, and also works part time to supplement her Social Security payments. He said to me, "Commissioner, how can we succeed in giving the best possible service to our beneficiaries, as you keep telling us to do, when the retirement earnings test, by its very nature, causes such problems for people and results in overpayments and underpayments to so many of them?"

The earnings penalty is the largest single cause of overpayments in the retirement and survivor's program. It accounted for over $500 million, or two-thirds, of the overpayments for 1986. Elimination of the penalty at the normal retirement age would save us considerable work years and close to $100 million per year in administrative costs.

Few people may argue the merits of eliminating the penalty. There are many who are rightly and properly concerned about the

costs involved in such an action, and clearly so are you and I. We all want to be fiscally responsible. We have been thinking about ways in which we can minimize the cost. Phasing out the earnings penalty rather than eliminating it immediately clearly substantially cuts short term costs.

There are a number of phaseout options, either phasing out the earnings penalty by lowering the age at which it applies, or alternatively, phasing out the earnings penalty by gradually increasing the annual exempt amount, perhaps over a 5-year period, which would immediately benefit all persons between age 65 and 69 who are affected by the test. Also, short term costs could be considerably less than if the test were phased out by age, because you have more leeway in deciding how to raise the annual exempt amount during that 5-year phaseout. You can raise it whatever amount you decide in terms of the dollars.

Still another option would be to increase the annual exempt amount by $3,000 or $4,000 for say 5 years, and then automatically adjust it thereafter. This type of approach deals with concerns that you, personally, have expressed that full elimination would help mainly higher earners.

There are several cost advantages that result if the earnings penalty were eliminated. The trust funds would clearly receive additional Social Security tax revenues, because beneficiaries would increase their work activity, and program savings would be generated through administrative savings as well. Further Medicare program savings would result, because many Medicare beneficiaries in the labor force are covered by employer provided health care programs.

I appreciate that there are other views on this subject, including those from the Congressional Budget Office and their statistical analysis of the future of this penalty. But I believe the effects of the retirement earnings penalty on the underground economy and on discouraging the work activity have been seriously underestimated and that eliminating the test will have a very strong positive effect on beneficiary work activity and will increase income tax revenues, in addition to also increasing FICA revenues.

In summary, I am, as you well know, strongly committed to finding a practical and a feasible approach for eliminating the earnings penalty at normal retirement age. It is a major work disincentive that does not any longer make sense for either the program or for our economy, and I firmly believe that the penalty can be eliminated in a way that satisfies cost concerns and meets the needs of beneficiaries who want to work. I hope that we can pursue that goal together.

Thank you.

Chairman JACOBS. Thank you, Ms. Hardy.

[The statement of Commissioner Hardy follows:]

DEPARTMENT OF HEALTH & HUMAN SERVICES
Social Security Administration
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STATEMENT

BY

DORCAS R. HARDY

COMMISSIONER

OF

SOCIAL SECURITY

HEARING ON

THE SOCIAL SECURITY

RETIREMENT EARNINGS TEST

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY

COMMITTEE ON WAYS AND MEANS

U.S. HOUSE OF REPRESENTATIVES

THURSDAY, SEPTEMBER 29, 1988

91-654 125

Mr. Chairman, I very much appreciate your invitation to appear before you today to discuss the Social Security retirement earnings test. I am pleased that you scheduled this hearing because the issue deserves public discussion.

I will start by giving a brief history of the test and a description of how it works today. Then I will discuss the pros and cons of retaining the test.

HISTORY OF THE TEST

The basic philosophy of the original Social Security program was that Social Security retirement benefits were intended to partially replace income lost due to retirement. The retirement earnings test was designed as an objective measure of the extent to which income is lost due to retirement. Thus, under the test, a beneficiary who continues to work after becoming entitled to Social Security benefits may lose some or all of his benefits, depending on his annual earnings.

The Social Security program has always had an earnings test, although it has changed quite a bit over the years. When benefits first became payable in 1940, a beneficiary lost his entire benefit for any month in which he earned $15 or more in covered earnings. The earnings test has been modified many times since then to:

- Convert the monthly test to an annual test;
- Broaden the scope of earnings countable under the test;
- Increase the amount of earnings that a beneficiary may earn without losing any benefits;
- Provide for a gradual reduction of benefits as earnings levels increase; and
- Establish an age at which beneficiaries are exempt from the test.

HOW THE CURRENT TEST WORKS

The earnings test reduces benefits by $1 for each $2 of earnings above the annual exempt amount. The annual exempt amount for 1988 is $6,120 for beneficiaries under age 65 and $8,400 for beneficiaries age 65 to age 69. These exempt amounts are adjusted annually to reflect increases in average wages. Workers are exempt from the test when they reach age 70. The test does not apply to disability beneficiaries, who are subject instead to a substantial gainful activity test, but it does apply to dependents of disability beneficiaries.

A worker's earnings above the exempt amount affect not only his own benefits, but also the benefits of family members receiving benefits on his earnings record. The earnings of a

dependent or survivor beneficiary can affect only that beneficiary's benefits.

Each year, about 1.4 million beneficiaries lose some or all of their benefits as a result of the test. Of this group, about 850,000 are retired-worker beneficiaries age 65 to 69 or dependents receiving benefits on the same record. About 350,000 are dependent or survivor beneficiaries who are affected by the test due to their own earnings.

ARGUMENTS FOR RETAINING THE EARNINGS TEST

Proponents of the test have generally presented the following arguments whenever the issue of eliminating the test has been raised:

- Eliminating the test would change the Social Security retirement program from insurance against the loss of income at retirement to an earnings based annuity payable upon reaching a defined retirement age.

- Eliminating the test would primarily advantage higher income beneficiaries because the current test affects the benefits of high earners to a greater extent than low earners.

- Current law already provides for further liberalization of the test. In 1990, the $1 for $2 benefit withholding rate above the annual exempt amount will be $1 for $3 for beneficiaries age 65 to 69.

- The test holds down program costs. If the test were entirely eliminated immediately, benefit payments could increase by about $11 billion per year.

- Eliminating the test would decrease the work incentive for some currently working beneficiaries now affected by the test since they could work less for the same amount of total income.

ARGUMENTS FOR ELIMINATING THE EARNINGS TEST

Those in favor of modifying or eliminating the earnings test have generally used the following arguments to support their position:

- Social Security benefits are an earned right--bought and paid for--and should not be withheld from eligible beneficiaries for any reason. The earnings test is a form of needs test which is inappropriate for an earned right program. Further, the annuity concept has already been established at age 70 since benefits are payable at that point regardless of earnings.

- The test discourages beneficiaries from working because the effective marginal tax rate on earnings--taking into account

the test itself, Social Security taxes, and Federal, State, and local income taxes--can approach 100 percent.

- By discouraging beneficiaries from working, the test deprives the country's labor force of the valuable skills and experience of older workers. As labor force growth slows, there will be labor shortages, and there is a need to encourage older people to participate in the labor force.

- The test encourages older workers to participate in the gray underground economy, especially those who are most in need of additional income.

- The test discriminates against those who depend on income from work rather than on investment income to supplement their benefits. Beneficiaries who have unearned sources of income--generally those at higher earnings levels--can receive their benefits without penalty.

- The cost of eliminating the test would be offset in part by additional Social Security taxes and income taxes attributable to increased labor force participation by older workers.

- The test is complicated, difficult to understand, and costly to administer. Elimination of the test could save about 2,500 workyears.

CONCLUSION

The Social Security program rests on the policies developed by the bipartisan National Commission on Social Security Reform and enacted in the Social Security Amendments of 1983. The Commission unanimously recommended that Congress "not alter the fundamental structure of the Social Security program or undermine its fundamental principles."

I have explained the arguments for eliminating the retirement earnings test. However, eliminating the earnings test now would cost the trust fund billions and would turn us away from the major policies adopted by the 1983 Commission and approved by the President and the Congress. The Social Security Administration is studying the effects of the earnings test on labor force participation of the elderly along with other critical issues affecting the retirement security of America's workers.

Chairman JACOBS. Ms. Wise has a question.

Ms. WISE. Yes. I just have one question. It has been mentioned many times already today that the labor supply would be increased if the retirement test were eliminated or phased out, yet there has been nearly a three decade trend of more people retiring early and indeed, the significant increases in the retirement test during the seventies did not result in an increase in the labor supply—that is, an increase in the number of people in the work force.

In addition, the Social Security actuaries have estimated that of the people eligible for Social Security who are 65 to 69, about 1 percent of those people would reenter the work force, or would continue working who would not otherwise work, 3 percent would increase their earnings, but 5 percent would actually decrease their earnings, because they, as a result are receiving the additional Social Security benefits. So there is a net decrease of 1 percent.

Can you tell us, or share with us, any additional data that you have that would demonstrate that the labor supply would actually increase—the number of people in the work force, the number of people continuing to work, or reentering the work force would actually increase as a result of eliminating the test?

Ms. HARDY. I do not have any further data than what you have discussed there. I do believe, in talking to people, the disincentive is so great no one even tries to work. They say Social Security, my Social Security, will be reduced; I am not going to work.

Second, the underground economy is so much greater than we give credit for in terms of data for the older senior citizen and that is clearly something that neither Treasury nor actuaries or anyone apparently is able to estimate.

Third is this whole concept of behavioral change. We could conduct numerous studies about it, but I am not even sure that people are going to tell us exactly how their behavior will change. I personally believe it will definitely change. What we have seen is where you have companies such as Travelers Insurance, which has done a major outreach to primarily their retired employees, but also older employees where they have processing and other plants, and other areas, they have reemployed a lot of those individuals.

Their studies have shown—and this is 1982—that 55 percent of the people that they have surveyed are very interested, or somewhat interested—in other words, would work additional time if it were not for the retirement earnings test. They have gone back to those people—even the ones who were currently working—and found that almost half of those would work more if it were not for the retirement test.

So you have two groups there—one that would work, the majority would work, and the other would work additionally. So I think we are starting to see a lot of private companies hiring people and coming up with great difficulties because they can't have the people back in the work force.

Ms. WISE. Thank you.

Chairman JACOBS. Commissioner Hardy, during your testimony you referred to the system you administer as the retirement and survivors program. What would you call it if we didn't have a retirement requirement any more?

Ms. HARDY. What would I call it?

Chairman JACOBS. You wouldn't call it a retirement program any more, would you?

Ms. HARDY. No. Just survivor's insurance. It would be less expensive.

Chairman JACOBS. How was that?

Ms. HARDY. Old age, survivor's.

Chairman JACOBS. You wouldn't call it retirement and survivors' program any more as you did extemporaneously a moment ago, would you?

Ms. HARDY. We could get into a clearly lengthy discussion of what exactly is retirement. Is retirement zero-work? Clearly, currently retirement is $8,400 worth of work, not $8,401 worth of work.

Chairman JACOBS. Would that be in the same genera as substantial gainful activity? Life is a relative matter, but at a certain point you know that you're substantially gaining and below that point.

Ms. HARDY. I think the Congress coined substantial gainful activity.

Chairman JACOBS. Probably in the same genera though, wouldn't it?

Ms. HARDY. Equally confusing, yes.

Chairman JACOBS. Are you big, are you small, are you this or are you that. Nonetheless, full time work is usually considered work. Less than that is considered part time work, and, at a certain point, under the Social Security system and under the contract under which people pay, the Social Security system retirement was pretty well defined, wasn't it, by the retirement test?

Ms. HARDY. It is defined by dollars, yes.

Chairman JACOBS. If you buy accident insurance——

Ms. HARDY. But only by dollars, clearly as earned income as opposed to any kind of dollars in unearned income.

Chairman JACOBS. That again, unearned by definition is not earning. It is not working, is it? You are not working when you have unearned income. That was the concept as I understand it.

Ms. HARDY. I am not the tax expert here, but it would seem to me there are ways through subchapters and whatever you could have income, and yes, you are not digging ditches as you talked about before, but you could clearly be receiving substantial income and talking on the phone or whatever kind of work one does in subchapters, and all sorts of things which give you cash.

Chairman JACOBS. The way I see it is you may have a lot of retirement income. All of it by its very nature is not currently earned. It is something that was earned earlier. You are retired when you clip coupons. Some people are luckier than others and some people are more prudent than others. I think it works both ways, but when you end up with that you are certainly not working. You can go play tennis, sit on the beach, and money comes in. Most employers wouldn't let you do that if you were considered in the work force and working.

Ms. HARDY. The concept, as you well know, is of the three-legged stool of pension, Social Security and savings being your base upon retirement at a particular age. If you have not been able to do as well as you should have and therefore you are on just Social Security and savings, and not a lot of coupons, then it seems to me that

the retirement earnings test does not give the person any additional choice to supplement, to add to, to give that opportunity and choice to the individual. As I said, there are different options as to how you can focus on this—but I think the $8,400 is just not only driving the underground economy, but also just not equitable.

Chairman JACOBS. Are there any other areas of Federal spending where you would advocate increasing entitlements besides this?

Ms. HARDY. No. I don't see it as an increase in an entitlement.

Chairman JACOBS. I wondered if you did.

Mr. Daub.

Mr. DAUB. I, for one—I know that we all do, Commissioner, appreciate your leadership on this issue. Can you say for the record what the public response has been to this initiative?

Ms. HARDY. The public response has really been overwhelming. I was just looking yesterday at the letters that we have received, that the President has received, that the chairman and that I have received—copies of letters to the chairman and to others—regarding "please eliminate this kind of penalty. I really do want to work and I am so mad about all the overpayments that I have to pay back," and such kinds of things, "you are being extremely intrusive in my life, and I should have the choice and ability, because it is good for me to continue to work."

When I do townhall meetings or talk with seniors around the country, it is very frustrating to them, and as Congressman Wyden pointed out, it is not necessarily the high wage earner. It is the person who is at the middle scale and even according to the CBO study, this kind of elimination would hit, would impact on, individuals who are under the $20,000–$25,000 threshold.

Mr. DAUB. Would you want to elaborate, or discuss the pros and cons of the phaseout approaches that have been taken by the bill that Mr. Archer has, the bill that I have? I know that your staff has done a lot of work on this and the question would be, is phasing out by increasing the threshold levels preferable to phasing out by age?

Ms. HARDY. We talked about, we all have talked about both. It appears to me that on the administrative side it is easier for us to do it by age, but it appears, because of the concerns about high wage earners that the increase in the dollar threshold might be more acceptable than the decrease in age.

The increase in dollars—in doing some analysis on our part—also costs a little bit less up to a threshold, in the $20,000–$25,000 range. It looks like about $3 billion over the first 5 years and clearly that divides, if it is equal, to about $600 million a year, and that, I should remind the committee, translates to one day's worth of Social Security benefits.

Mr. DAUB. When FDR signed the bill as the basis for our system, which I believe underpins the stability of middle America—that is what Social Security is worth, in my opinion—he said it is a great day for the country. There will never be another person on welfare.

He went on to describe the three legged stool theory, if you go back and read the words.

Churchill said, "if you know history, you can make history. If you ignore it, you do so at your peril." The fact of the matter is, if there are so many screams out there in America about health care

and home health and long term nursing home care, and how can people save, then we have got to give them every reason in the world during their productive years—however many of them they may be blessed to have—to save for those unexpected things that occur, particularly in older life.

It would seem to me whether one is a rich or poor or middle income American, that that limitation is just as onerous as was the retirement age.

Why shouldn't we take the opposite approach if we have this limitation, why shouldn't we extend the retirement age if we are healthier and living longer? Why shouldn't the limitation be 75 and we keep this penalty in effect until 75? Isn't that logical if we are going to continue to defend it based on the same rationale? Shouldn't we really raise the age against which the limitation continues to apply rather than eliminate it?

Ms. HARDY. Well, if we want to defend it, that is certainly one way to go. But I think that the extension of the earnings limitation does not take account of the present discussion. It would not take into account the future needs of the economy and what we are going to need in this country also with regard to workers, in general, and specifically the skills and talents and opportunity for the older worker.

The changes that we foresee by the year 2000 are just monumental. We expect that we will need these older workers and we believe they should have that opportunity to participate. Again, that doesn't even take into account the behavioral changes. For example, the Travelers studies show that the individuals who do work are healthier, they are more productive, they do an excellent job, they have less problems in terms of socialization, et cetera. And really private industry has seen that this is a real plus for these kinds of workers in the work force.

Mr. DAUB. There are over 50 Members from both parties of Congress who have sponsored or cosponsored bills to do something about this limitation. The Senate has a bipartisan bill, 11 current cosponsors. It seems to me there is developing an awareness that something should be done.

I read former Chief Actuary Robert Myers' statement last night. There were two comments in it. I would like your reaction:

First, as an incentive to delay retirement and offset initial program costs, continue to offer the delayed retirement credit past age 70.

Ms. HARDY. I had not thought about that. I would have to ask the actuaries to do some calculations as to what kind of impact that would have. Actuarially I am told the 8 percent is fair, which would come in at age 65. We could certainly look at that.

Mr. DAUB. And he said, retain the current recomputations for years after a beneficiary first files for benefits, because it is unfair to place persons in the position of having to make that decision before he or she really knows what the long term differences in benefits would be.

Ms. HARDY. Well, I believe that if we are going to increase substantially the retirement earnings test limit and hopefully eliminate it, that you should make a decision with the increased DRC—the delayed retirement credit.

So say you decide to work and take benefits starting at 66 or 67. I would not support keeping the recomputations after that. I think you make that decision to start getting benefits and then, if you work after that, you, as all workers, would continue to pay Social Security taxes but without the recomputing of your benefit every year. I would rather have those dollars, small dollars in terms of recomputations go into offsetting the cost of the elimination of the test.

Mr. DAUB. Mr. Archer's bill does eliminate recomputations.

Ms. HARDY. Yes.

Mr. DAUB. What about if we keep the limitation and simply give that worker some sort of credit for the choice that he makes to delay taking out benefits from the trust fund, give him a break in the opposite way. Have you ever thought about the idea if they are learing enough to file an income tax return, give them some kind of a lump sum credit, an extra dependent exemption or something?

Ms. HARDY. We have not looked at that. I think, primarily, because there is enough discussion with the statistical analysis around town and Department of the Treasury and others. But we certainly could try our hand at that.

Mr. DAUB. I appreciate your commitment to this issue and hope that it blooms in some way next year.

Chairman JACOBS. The Chair thanks you for your contribution.

Ms. HARDY. Could I just comment it has been a pleasure to work with Congressman Daub and we will miss him next year.

Mr. DAUB. I am going to miss you, too.

Ms. HARDY. I hope we too will be able to be successful.

Thank you.

Chairman JACOBS. The entire subcommittee has the same feeling. We don't miss him altogether, he won't be too far away. We are personally very fond of our colleague.

Ms. HARDY. Thank you, Mr. Chairman.

Chairman JACOBS. Dr. Flemming, you are on deck.

STATEMENT OF ARTHUR S. FLEMMING, COCHAIR, SAVE OUR SECURITY COALITION

Chairman JACOBS. Dr. Flemming, as usual, you are welcome to the committee.

Mr. FLEMMING. Mr. Chairman, Mr. Daub, thank you very much. I appreciate the opportunity of appearing before you, appearing on the retirement test.

First of all, I want to express my appreciation over the fact that the committee is confronting this issue. I know from my own experience that it is a very live issue and I know, as a result of my current experiences, traveling throughout the country, that it is an issue that is on the minds of a good many persons.

I would like to approach the issue from the standpoint of impact on our overall Social Security system:

First of all, right at the outset, I would like to suggest that this is the type of issue that personally I feel should be considered by the next Social Security Advisory Committee in connection with other recommendations that have been or will be made for changes in our total Social Security system. We know that the system is in

close actuarial balance. We know, therefore, that any changes in benefits will have to be accompanied by increases in revenues.

Personally, I appreciate very much the report of the Congressional Budget Office. It seems that they lay out the issue in a very effective way and that they also identify very effectively the costs that are involved in connection with the various options.

I feel that the proposed change in benefits should be considered at the same time that the merits of other proposed changes in benefits are considered and choices should then be made in the light of specific recommendations for increases in revenues.

This is a task that historically has been undertaken by Social Security Advisory Boards and these recommendations have been found to be helpful by both the executive branch and the Congress. The process involved in the Social Security Advisory Board approach helps us to avoid the temptations of a patchwork approach.

I recognize that the retirement test was made a part of the Social Security system at the outset in order to answer the question when has a person retired, and is therefore eligible to begin drawing benefits. In the early days of the system it was a very stringent test. Beginning in the fifties, a policy was put into effect of gradually liberalizing the system.

The Secretary—I participated in helping to implement such a policy. That policy of liberalization continues. For example, as a result of Congress taking a look at the total system in 1983, beginning in 1990 benefits will be reduced by one dollar for every three dollars instead of two in excess of the earnings ceiling for persons who reach full retirement age.

Now, the costs involved in that liberalization were considered in connection with the amendments of 1983, taken into consideration by the actuaries, and revenues that have been built into the system are adequate to take care of that particular liberalization of the retirement test.

In this connection, I think we should keep in mind that the delayed retirement credit, which is now 3 percent a year, beginning in 1990 will increase gradually each year until it reaches 8 percent in 2009 and thereafter.

Of course, there are increased costs involved in that which are taken into consideration in connection with the 1983 amendments.

I recognize that reasonable persons can differ on the impact that the earnings test has on older persons responding to opportunities for continued involvement in the work force. We haven't really had in-depth studies on that particular aspect of the problem. Nevertheless, at this point, I believe that we must keep in mind that we are dealing with an insurance program and not a pension program. The report of the Congressional Budget Office points out very clearly that there are two schools of thought in this country—those who regard the retirement part of our social insurance program as an insurance program, as social insurance.

Then there are those who regard it as a pension program. It seems that the legislative history makes it very, very clear that it is an insurance program. This means that we must be able to apply some test to determine when people have retired and are entitled to benefits.

I read with a great deal of interest the interview that correspondent for the New York Times conducted with you, Mr. Chairman, in the early part of January. He likewise conducted an interview with Commissioner Hardy on this issue. I felt your replies were very, very consistent with the legislative history of Social Security—namely they were consistent with the fact that this is an insurance program and not a pension program.

Oftentimes when I am talking with people out in the field I say that it is an insurance program. It is not an annuity program. I mean to draw the distinction. Because of that, I again say we must be able to apply some test to determine when people have retired and are entitled to benefits. If we accelerate the liberalization of our present test, we are going to have to spend more for benefits than we are now spending. The Congressional Budget Office report makes that very clear. Obviously we would have to spend a great deal more if we eliminate the retirement test.

I think the question that you addressed to Commissioner Hardy is very relevant. If we eliminate it, then what do we have here? What is this? What are we going to call it? No longer is it an insurance program designed to deal with loss of income when people retire.

But if we are going to accelerate the liberalization, the liberalization already built into the law—as I have indicated, the 1983 amendments constitute very significant liberalization of the test. But now if we are going to accelerate it, it is going to cost us more. We have the cost estimates in front of us.

It seems to me that this means that surely the bills that would direct this liberalization should also contain some provision for additional revenues in order to cover the costs. Because if they do not, then we clearly are going to disturb the close actuarial balance of the system.

I do not believe that either policy is a wise policy to follow at this time. We know that there is a well organized, as well as financed, group in our nation who contend that we cannot solve our overall fiscal problem without cutting Social Security benefits. I am in complete disagreement with those who contend that that is the case. But I do not want to see us play into their hands by adding an increase in benefits here and there, so as to give them the opportunity of adding them up and saying that the present program for financing the system is inadequate and therefore, one of the ways to deal with it is to cut Social Security benefits in order to bring it into balance.

That is why, it seems to me that when matters of this kind are addressed, we must address the revenue side of it, and where we are going to get the revenue. I have appeared before this subcommittee on one or two other proposals that have involved increases in expenditures under the system and taken the identically same position.

That is why I again suggest that this item be placed on the agenda today for the next Social Security Advisory Group. Then its merits and its demerits can be considered alongside the merits and demerits for other proposals—for example, proposals to deal with the inequities that are built into the system insofar as women are concerned—that group can then advise the executive branch and

the Congress as to what they feel can be done at that particular point to improve the system and where the money is going to come from in order to keep it in close actual balance.

Thank you, Mr. Chairman.

[The statement of Mr. Flemming follows:]

OUTLINE OF TESTIMONY
By
Arthur S. Flemming

I. Introduction

A. I appreciate the opportunity of participating in this hearing on the retirement test.

B. First of all I would like to suggest that this is the type of issue that should be considered by the next Social Security Advisory Committee in connection with other recommendations that have been or will be made for changes in our total Social Security System.

1. We know that the System is in close actuarial balance.

2. We know, therefore, that any changes in benefits will have to be accompanied by increases in revenues.

3. But the merits of any proposed change in benefits should be considered at the same time that the merits of other proposed changes in benefits are considered and choices should then be made in the light of specific recommendations for increases in revenues.

4. This is a task that historically has been undertaken by Social Security advisory bodies and these recommendations have been found to be helpful by both the Executive Branch and the Congress.

5. The process involved in the Social Security advisory body approach helps us to avoid the temptations of the patchwork approach.

6. The next Social Security advisory council is scheduled to be convened in 1991.

II. Body

A. I recognize that the retirement test was made a part of the Social Security System at the outset in order to answer the question: When has a person retired and is therefore eligible to begin drawing benefits?

1. In the early days of the System it was a very stringent test.

2. Beginning in the 1950s a policy was put into effect of gradually liberalizing the System.

3. The policy of liberalization continues. For example: Beginning in 1990, benefits will be reduced by one dollar for every three dollars (instead of two) in excess of the earnings ceiling, for persons who reach full retirement age (65 in 1990).

4. In this connection we should keep in mind that the delayed retirement credit, which is now 3% a year, beginning in 1990 will increase gradually each year until it reaches 8 per cent in 2009 and thereafter.

B. I recognize that reasonable persons can differ on the impact that the earnings test has on older persons responding to opportunities for continued involvement in the workforce.

C. Nevertheless, at this point I believe that we must keep in mind that we are dealing with an insurance program and not a pension program.

1. This means that we must be able to apply some test to determine when people have retired and are entitled to benefits.

2. If we accelerate the liberalization of our present test we are going to have to spend more for benefits than we are now spending.

3. This means that we must increase our revenues or disturb the close actuarial balance of the System.

4. I do not believe either policy is a wise policy to follow at this time.

III. CONCLUSION

A. I again suggest that this item be placed on the agenda for the next Social Security Advisory group.

B. Then its merits and demerits can be considered alongside the merits and demerits for other proposals for change.

Chairman JACOBS. Mr. Daub.

Mr. DAUB. Do you think that it is a meritorious concern? In other words, you say that the Commission should look at it and that it should be put in tandem, should be looked at, dovetailed with other changes that might be contemplated? I assume you mean the revenue implication in total should be looked at not just piecemeal?

Mr. FLEMMING. That is correct.

Mr. DAUB. If you were on the committee, do you think this is something we ought to adjust or something we ought to leave alone?

Mr. FLEMMING. This is something that I would consider, but I would balance it over against the kind of an issue that I just suggested—the equities that have been built into the system as far as women are concerned.

I would feel that I was in a position where I undoubtedly would have to do some—would have to give it a priority rating of some kind. As between the two, as between this and the one I just identified, I wouldn't give this as high a priority rating as I would dealing with some of the inequities that have crept into the system as far as women are concerned. But it is that kind of a process that I think we ought to through.

Let me be very frank. When I took office as Secretary of HEW, one of the first issues that was presented to me was this issue. Now, I happen to be a person who has been trying to crusade in season and out of season, open up opportunities for older persons to continue to be involved in life, involved in full time employment, part time employment, involved as volunteers, because I believe noninvolvement can lead to rapid physical, mental and spiritual deterioration.

I believe our society should do everything we possibly can to open up these opportunities. I did see in this test a possible deterrent. So I raised the issue with the Social Security Administration, with the staff and so on, and they very quickly put me through a training program in terms of why this was brought into existence in the first place and what the cost implications would be. And they asked me then, at that time, if you had thought about eliminating it, it would have been a very costly operation.

We had a lot of other defects in the system and they asked me to balance one over against the other. Well, I did, and I concluded that this was not entitled to as high a priority as I thought it was, but at that time, we did agree with one another, let's continue this process of liberalization. And I supported the process of liberalization.

I supported what Congress did in 1983. That was a good step in the right direction. I don't think it should be pulled out now and just considered by itself, and certainly should not be considered by itself without considering some possible opportunities for additional revenue.

Mr. DAUB. If we had more time, I would explore. We have a vote on right now. I would certainly hope maybe after this hearing, or some future date, you might tell me who those well-organized and powerful people are that are out there to cut social security.

Mr. FLEMMING. I would be glad to discuss that with you.

Mr. DAUB. Maybe Mr. Strauss or somebody like that. I don't know who you are referring to.

Mr. FLEMMING. I have some other names in the back of my mind. They are pretty well known as a result of ads that they have inserted from time to time in the Washington Post and so on.

Chairman JACOBS. We thank you, Dr. Flemming, for your contribution. As usual, it was very useful.

There are three more panels. I would like to take a vote whether you would rather break for lunch or come back directly. Those who are scheduled to testify who would like to come back directly, please raise your hands.

Those who feel otherwise, raise your hands.

We will come back directly.

[A short recess was taken.]

Chairman JACOBS. I would ask our next panel to come forward. Stephen J. Entin, resident scholar, Institute for Research on the Economics of Taxation; and Wayne Vroman, senior research associate, the Urban Institute.

STATEMENT OF STEPHEN J. ENTIN, RESIDENT SCHOLAR, INSTITUTE FOR RESEARCH ON THE ECONOMICS OF TAXATION

Mr. ENTIN. I appreciate the opportunity to discuss the Social Security earnings test with you. Prior to joining the Institute for Research on the Economics of Taxation, I was Deputy Assistant Secretary for Economic Policy, U.S. Treasury Department. In that capacity, I worked for 7 years with the Social Security Administration on the annual trustees reports and other matters pertaining to the system.

The rate at which benefits are reduced by the earnings test is scheduled to fall to $1 for every $3 of excess earnings in 1990, but only for beneficiaries at or above normal retirement age. As the normal retirement age is raised from 65 to 67 in stages after the turn of the century, the reduction will revert to $1 in $2 for those ages 65 and 66.

The administrative burden of the provisions have been reviewed by Commissioner Hardy. I would like to focus on the economic impact of the provisions.

The one-for-two benefit reduction is equivalent to a 50-percent marginal tax rate on a beneficiary's earnings in excess of the exempt amounts, until the excess earnings build to more than twice the Social Security benefits and all benefits have been lost. On top of this must be added other tax rates facing the working beneficiary.

This routinely results in marginal tax rates of 65 to 85 percent on added earnings for retirees of modest income. When coupled with the phase-in of the taxation of benefits, which imposes an additional tax spike on other retirement income, marginal tax rates can easily exceed 100 percent for persons with $30,000 to $40,000 in total income.

Parenthetically, let me note much the same effect of sheltering lower-income taxpayers from the taxation benefits could have been achieved without this tax spike on other retirement income by al-

ternative methods of benefit taxation. The committee may want to explore this problem at some other time.

The delayed retirement credit affects the situation with the earnings test. Some claim it is to be regarded as an offset to the penalty of the test. However, the credit is far too small to offset advantages of early retirement built into the benefit computational rules, let alone to offset the severe penalty of the earnings test itself.

Under current law, the delayed retirement credit is being increased in stages to two-thirds of 1 percent per month or 8 percent per year for those reaching age 62 in 2005 and beyond. This is an actuarially fair level which will make the retiree able to work several extra years and collect the same lifetime benefits in terms of present value as if the earnings test did not apply. In fact, the earnings test would then cease to affect the amount of benefits paid and influence only their timing. At that point there would be no added cost from ending the earnings test, and so the cost of doing so earlier than the year 2005 would be temporary. But this is 17 years away, and it does nothing to address the current problem faced by current retirees.

SSA estimates that something in excess of 400,000 or 500,000 people are exposed by the earnings test to a range of marginal tax rates between 65 and 85 percent. Repeal of the earnings test would reduce their marginal rate to a range of 15 to 35 percent. This would raise their after tax wage at the margin by 150 to 300 percent. It would not be at all surprising, given any kind of normal labor supply response, to see an increased amount of work effort by members of the affected group.

It has been suggested some allowance should be made for reduced work effort for people who work in spite of the earnings test and who would get a windfall from the earning test repeal. I am very skeptical this would be a large effect. There is confusion there between the one-time lump sum payment and the effect of that payment on the individual's lifetime earnings carried out beyond the point when he does in fact cease to work. For example, getting a rise in benefits of $5,000 for 1 year, if spread over a retirement of 10 years after all work ceases, is really a permanent income gain of only about $500 a year, not much incentive to quit working.

Very conservative estimates along these lines by Social Security, including added work by some retirees and less by others, has indicated one might expect additional earnings of $0.5 billion to $1 billion by the affected group if repeal were done for ages 65 through 69. Such earnings would produce additional revenues from taxation of benefits of between $0.1 billion and $0.2 billion per year and between $0.1 billion and $0.2 billion in additional income and payroll tax revenues. This would each offset about 5 percent of the cost of repealing the earning test for this age group. I believe the estimates on the work effort and reflow from taxation of higher earnings are low possibly by a factor of up to five or thereabout. I have seen estimates that range much higher, over 50 percent reflow.

It should be noted that any revenue estimates the subcommittee may receive on the tax consequences of eliminating the earning test from the Joint Tax Committee, CBO or Treasury will likely include only the revenue from the direct taxation of added benefits paid out. The estimate will be unlikely to include any revenues due

to higher employment and earnings of the elderly as a result of the repeal.

Each agency, as a matter of policy, sticks to an unchanged economic baseline forecast. Real world changes in GNP and associated income changes due to a policy shift are ignored. This exaggerates the cost of making desirable policy changes. The committee should be aware of this practice.

Failure of the revenue estimators to adjust receipts for changes in the economy may not be particularly damaging in this instance; it would matter much more, however, were the committee to consider repeal of the earnings test for persons age 62 through 64, where continuation of previous full-time employment at higher wages is more likely than at an older age. It would matter more in consideration of other tax changes on the working age population and in the tax treatment of capital where revenue reflows can be substantial. Capital gains is a case in point.

Repeal of the earnings test, as indicated, is most often discussed for ages 65 through 69, where complete repeal would cost $5 billion in higher benefit outlays, not counting offsets. As mentioned above, SSA might indicate a 10-percent reflow recovered through higher taxation of benefits and higher income and payroll taxes, and the real offset could go much higher. There are several minor adjustments to the benefit computation process, some of which Commissioner Hardy has gone over with you, that might be employed to provide additional savings. I mentioned several in the full testimony which I will submit for the record, which would perhaps cover another one-third of costs. Combining these offsets would cover half of the cost of the repeal.

A phase-in of the reform could make the task much easier. For example, eliminating the limit for workers at age 69 in 1989, age 68 in 1990, and so on would cost under $1 billion the first year, rising in stages to the full $5 billion in 1993. During this period normal real economic growth will be raising real Federal revenues by about $30 billion each year or by over $150 billion annually by 1993. To implement this reform would take only a bit over 3 percent of the real growth of revenues over 5 years.

I feel consideration should also be given to eliminating the earning tests for those below normal retirement age. There would be more recovery of costs from added work effort and tax payments from this group. This would increase the cost of repeal, but a phase-in could cushion the impact. Perhaps the early retirement penalty or basic benefit formula could be adjusted to defer part of the costs, but such steps could only be taken with many years' warning to give people time to plan additional saving or to plan for an additional 3, 4 or 5 months of work to make up for the difference.

Much will undoubtedly be made of the distribution of benefits across income classes under repeal of the earnings test. This is not the way to view the proposal for several reasons:

No taxpayer should have to face routinely tax rates of 65 to 85 percent, let alone rates over 100 percent. This is virtually a Federal order of forced retirement and is contrary to recent legislation in that area, including tax reform.

Progressivity should be addressed in the basic structure of exemptions and tax rates, not piecemeal in obscure corners of the Tax Code and entitlement programs. No one devising a new Tax Code and income transfer system for the country would handle the problem with a peculiar penalty on persons age 62 to 69.

While repeal may provide additional benefits to upper-income persons, they are likely to be taxed to a greater degree.

Finally, there are already too many peculiar spikes in the tax and entitlement programs, including rapid loss of welfare benefits as earnings rise, the sharp phaseout of the earned income tax credit, the phase in of Social Security benefit taxation, the tax-based premiums charged for the catastrophic coverage in medicare, and the 5 percent surcharge eliminating the 15 percent bracket and the personal exemptions for upper-income taxpayers, which raises the top tax rate to 33 percent for that group.

In conclusion, it would be extremely beneficial from an economic, tax simplification, administrative, and personal liberty standpoint to repeal the Social Security earnings test. Budget and distributional concerns are minor by comparison with the benefits to be had from this reform and can be dealt with via phased reductions and other adjustments to the benefit computation rules.

[The statement of Stephen J. Entin follows:]

Social Security Retirement Earnings Test

Statement of

Stephen J. Entin
Institute for Research on the Economics of Taxation

before the

Committee on Ways and Means
Subcommittee on Social Security

September 29, 1988

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to discuss the Social Security retirement earnings test with you. Prior to joining the Institute for Research on the Economics of Taxation, I was Deputy Assistant Secretary for Economic Policy, U.S. Treasury Department. In that capacity, I worked for seven years with the Social Security Administration on the annual Trustees Reports and other matters pertaining to the System.

The retirement earnings test does a great deal of harm, and very little good. It is unpopular with the public as an infringement on personal liberty, and with the civil service as an administrative nightmare. It is economically counter-productive, and will become more so as time goes on. It lingers primarily because of concerns over the budget impact of its removal, yet that impact is not measured or reported accurately to the Congress, and should not, in any event, stand in the way of fixing a truly perverse policy. It should be possible to find an acceptable schedule for the gradual elimination of this provision within budget constraints.

How the test operates.

The earnings test reduces social security benefits by $1 for every $2 of wage and salary income earned by the beneficiary above exempt amounts. In 1988, the exempt amounts are $6,120 for beneficiaries under age 65, and $8,400 for beneficiaries age 65 through 69. These amounts are adjusted each year by the growth of average wages in covered employment. Those over age 69 are not subject to an earnings limitation. Income from savings or pensions is not subject to the test, which is meant to be a test of retirement, not a means test. The rate of benefit reduction is scheduled to fall to $1 for every $3 of excess earnings in 1990, but only for beneficiaries at or above normal retirement age, currently 65. As the normal retirement age is raised from 65 to 66, and from 66 to 67 in stages for people reaching age 62 between the years 2000 and 2005, and 2022 and 2027, respectively, the reduction will revert to $1 for every $2 of excess earnings for those ages 65 and 66.

Compliance problems and administrative burden.

Beneficiaries are supposed to inform the Social Security Administration (SSA) each December how much they expect to earn over the coming year, along with actual figures for the year just past. SSA is then supposed to reduce or eliminate their monthly benefits accordingly for the year ahead, and correct for any misestimate of earnings and resulting incorrect benefit adjustment during the prior year. In many cases, beneficiaries either do not know of the provision, or estimate incorrectly, or simply

fail to report. Incorrect estimates have to be corrected via lump-sum payments or refunds, with possible complications with respect to income taxation of benefits, including amended income tax returns and administrative costs for the Internal Revenue Service as well as SSA.

In the case of non-filing or deliberate non-compliance, SSA must initiate recovery proceedings. SSA must run a computer match each year between beneficiaries' payment records and workers' annual earnings reports, which consist of W-2 forms provided by employers and the schedule SE's filed by the self-employed with the IRS at tax time to determine if any beneficiaries who have excess earnings have received excess benefits. It must then bill the beneficiaries for excess benefit payments, or, if reduced benefits are still being paid, reduce them further to recoup earlier overpayments. These adjustments are inconvenient for the beneficiaries and impose a non-trivial administrative cost on SSA, offsetting a portion of the savings in benefit payments attributable to the earnings test. SSA estimates this expense to be about $200 million annually, with about 40 percent of that cost attributable to dealing with adjustments for persons age 65 through 69.

Effect on marginal tax rates.

The one-for-two benefit reduction is equivalent to a 50 percent marginal tax rate on a beneficiary's earnings in excess of the exempt amounts, until the excess earnings build to more than twice the social security benefits and all benefits have been lost. On top of this must be added other tax rates facing the working beneficiary. Chief among these are the marginal federal income tax rate, the payroll tax rate, and the marginal state income tax rate. (Others, not factored into this analysis, include federal and state unemployment taxes, welfare benefits subject to phase-out with income, and the income tax surcharge implicit in the tax-based premium for catastrophic health insurance under medicare.)

When the various taxes are imposed together, marginal tax rates can get to be extremely high at moderate income levels. A married couple age 64 with total income of $10,000 could face a 65 percent marginal tax rate. A couple age 65 with total income of $18,000 could face a marginal tax rate of 81 percent. At higher incomes, with benefits reduced to zero, the marginal rates would be lower.

	single retiree	married couple	
	age 65	age 65	age 64
income from:			
pension	$ 1,000	$ 1,000	$ 0
savings	1,000	1,000	0
wages	8,400	8,400	6,120
social security	6,000	8,000	4,000
total income	$16,400	$18,400	$10,120
tax on added dollar of wage income from:			
benefit reduction	50%	50%	50%
federal income tax	15	15	0
payroll tax (self-empl.*)	13.02	13.02	13.02
state income tax	3	3	2
total marginal rate	81.02%	81.02%	65.02%

* The examples incorporate the 1988 self-employed payroll tax rate, 15.02 percent less a 2 percent credit, or 13.02 percent. This is close to the combined employer-employee rate after allowance for deductibility of the employer's share. The combined rate is the true measure of the tax burden on the gross wage.

Interaction with income taxation of social security benefits.

As taxpayers move toward the upper end of the 15 percent tax bracket or the bottom of the 28 percent tax bracket, most would have sufficient social security income to trigger taxation of benefits. Their added wage income would then be subject to both the earnings limitation and the effects of benefit taxation.

To keep benefits of lower income persons exempt from tax, the 1983 Social Security Amendments provided that benefit taxation begins when the sum of a beneficiary's adjusted gross income, tax exempt bond income, and half of social security benefits exceed $25,000 for a single beneficiary and $32,000 for a married couple filing jointly. These amounts are not adjusted for inflation, and will affect more beneficiaries each year at lower real incomes. For each dollar by which this sum exceeds the exempt amounts, $0.50 of the taxpayer's social security benefit becomes taxable income, up to half of benefits. During this phase-in range, the effect of earning an added dollar of interest or wages is to increase taxable income by $1.50, effectively raising the marginal tax rate on the added dollar of wages or interest by half, e.g., from 15 percent to 22.5 percent or from 28 percent to 42 percent. This is an unfortunate tax penalty on private saving for retirement.

Much the same effect of sheltering lower income taxpayers from taxation of benefits could be achieved quite simply, and without this tax "spike" and interactive penalty on other retirement income, by an alternate method of benefit taxation. Some amount of benefits, say, $4,000 for a single retiree, $6,000 for a couple using a 50 percent spousal benefit, and up to $8,000 for a couple with independent benefits, could be made tax exempt. Any benefits in excess of the exempt amounts would be taxable, up to half of benefits.

When a beneficiary is subject to both the earnings test and the phase-in of benefit taxation, the interaction of the two provisions produces an effective increase of 37.5 percent in the marginal tax rate on wage and salary income, rather than one-half. (The added dollar of wages costs the beneficiary $0.50 in benefits, half of which applies toward the threshold of benefit taxation. The net result is an additional $0.75 in income above the threshold, and an additional $0.375 in benefits' becoming taxable. Thus, the consequence of the added dollar of wages is to raise taxable income by $1.375.) This effectively raises the 15 percent tax rate to 20.625 percent, and the 28 percent tax rate to 38.5 percent. Marginal tax rates under these conditions can exceed 100 percent.

	single retiree age 65	married couple age 65
income from:		
pension	$9,000	$12,000
savings	5,000	7,000
wages	8,400	8,400
social security	8,000	12,000
total income	$30,400	$39,400
tax rate on added dollar of wages from:		
benefit reduction	50%	50%
federal income tax	38.5	38.5
payroll tax (self-employed)	13.02	13.02
state income tax	4	4
total marginal rate	105.52%	105.52%

These highest marginal tax rates, illustrated above, do not apply to large numbers of people; an area of potential overlap between the phase-in of taxation of benefits and the effective range of the earnings test occurs at the margin for a limited number of taxpayers. ("Potential" because one would not expect many taxpayers to permit themselves to be subjected to such confiscatory treatment.) For example, a couple with $12,000 in benefits would lose those benefits as wage or salary income rose from $8,400 to $32,400, scarcely above the threshold for benefit taxation in the absence of income from savings. With income from savings, the affected amounts would be far larger, and the tendency to reduce earnings far greater. Thus, there would be many more individuals facing possible effective marginal rates in the 65 percent to 85 percent range than in excess of 100 percent. Nonetheless, the possibility of such rates must distort decision-making unnecessarily for many people, and is bad tax policy.

Effect of delayed retirement credit (DRC).

Basic retirement benefits are calculated as of the normal retirement age, currently 65. Those retiring earlier have their benefits reduced by 5/9 percent for each month of retirement before age 65, an early retirement penalty (ERP). Those retiring later than the month of attaining age 65 have their benefits increased by 1/4 percent per month for each month retirement is delayed past age 65. Those whose benefits are reduced in any month by the earnings test receive an increase in their future benefits of a similar 1/4 percent for each month the earnings test applied, beginning once their earnings have dropped below exempt amounts. This provision of the DRC is sometimes cited as an offset to the adverse effects of the earnings test. However, the contention is not valid for several reasons.

The DRC acts as a partial offset to the incomplete indexation of workers' earnings histories in determining initial retirement benefits (primary insurance amounts, or PIA's). A retiring workers' earnings are indexed up until age 60. These indexed earnings are added to unindexed earnings through age 62, 65 or any later retirement age in determining average lifetime earnings and PIA's. Furthermore, any earnings after retirement which go into a recomputation of benefits are not indexed. Thus, delayed retirement means giving up indexation of a portion of the wage history, resulting in lower replacement rates the longer one delays retirement. The DRC at current levels is a partial adjustment for that problem.

The current DRC is not adequate on an actuarial basis to make the present value of expected lifetime benefits under delayed retirement equal to the expected benefits received by retiring at age 65 (or age 62, in spite of the ERP). Under current law, the DRC is being increased in stages to 2/3 percent per month for those reaching age 62 in 2005 and beyond. This will make the annual increase in benefits from delayed retirement equal to 8 percent per year. Under current interest rate and life expectancy assumptions, this should make the present value of expected benefits equal whether one retires at age 65 or later. This sort of average, of course, would not work well for someone who dies earlier than the average retiree, and might not completely compensate a risk-averse population, but it would go a long way toward reducing the work disincentive from the earnings test. One could work several extra years and still collect the same lifetime benefits. The earnings test would then cease to affect the amount of benefits paid, and influence only their timing. The earnings test could then be eliminated for those 65 and over with no meaningful budget consequences. However, this is seventeen years away, and does nothing to address the current problem.

Effect on work effort.

Repeal of the earnings limitation would produce two general types of effect on the work effort of retirees. One is a relative price effect: removal of a steep marginal tax would raise the after tax wage received for an added hour of work, thus increasing the amount of goods that could be bought with an added hour's wage. This raises the relative price, in terms of goods and services foregone, of an added hour of leisure, and encourages people to work more. The other effect is an income effect: an increase in income, other things equal, enables people to purchase more leisure. Normally, relative price effects of price and tax rate changes dominate income effects.

Someone experiencing a pure income effect, such as by receiving a bequest which produces considerable interest income each year, with no increase in the wage rate to encourage added work effort, might be expected to reduce work effort and take more leisure. The income effect, however, usually refers to a permanent change in income. A lump sum received on one occasion is not the appropriate measure of the impact on behavior; rather, the interest that could be received on the sum indefinitely is a better guide.

There are a bit over 8 million retirees age 65 through 69. Roughly 6 million report no earnings. Another million have earnings well below the levels at which the earnings test applies, and are generally assumed not to be affected. Of course, some might have chosen to remain in a job which could not easily accommodate part time work, and which would have paid a considerable minimum income, if the test were not in place.

Some 600,000 retirees who have filed for benefits have earnings in excess of the limits set under the earnings test, with benefits partially or entirely withheld. Of these, about 400,000 have benefits partially withheld, or have earnings just a bit more than sufficient for total loss of benefits. These are the people most likely to respond to elimination of the earnings test with added work effort, as its repeal would sharply raise the reward to added hours of work.

About 200,000 retirees have filed for benefits, but have earnings well beyond the point where benefits have been reduced to zero, and do not face the add-on 50 percent penalty on added earnings. In the event of repeal of the earnings test, these retirees would receive a lump sum increase in income due to the restoration of the lost benefits, which might induce some decrease in work effort. However, lump sum increases of this type should not affect expected lifetime income or work effort to any significant degree.

Another 600,000 retirees have high earnings, and have not chosen to file for benefits, in some cases because there would be none forthcoming after the earnings test adjustment. They too might reduce work effort slightly due to higher income if the test were repealed, and might file for benefits.

Among the roughly 400,000 people exposed to a range of marginal tax rates between 65 and 85 percent, repeal of the earnings test would reduce their marginal rates to a range of about 15 to 35 percent. This would raise their after tax wage at the margin by about 150 to 300 percent. It would not be surprising, given normal labor supply responses, to see an increase in work effort and earnings on the order of 50 to 100 percent by members of the affected group. However, some among the elderly may have medical reasons for only working part time, and others may have diminished attachment to the workforce for other reasons, resulting in a smaller response. Perhaps 200,000 to 300,000 individuals would work significant extra hours.

Very conservative estimates by SSA, including a large negative income effect, suggest additional earnings of $0.5 to $1.0 billion per year by retirees age 65 through 69 in the event of repeal, producing additional revenue from taxation of benefits of between $0.1 and $0.2 billion per year, and between $0.1 and $0.2 billion in additional income and payroll tax revenues. Each effect would offset about 5 percent of the cost of repealing the earnings test for this age group. Without the questionable large negative income effect, reflow from taxation of earnings could exceed 50 percent or more of the higher benefits paid.[1]

There are two reasons for doubting that income effects will seriously reduce the work effort of elderly beneficiaries:

-- First, in the case of workers whose earnings are high enough to result in total loss of benefits, it is true that repeal of the test would result in a lump sum gain in income with no increase in the marginal wage. However, even if the lump sum is large relative to the current year's earnings, it may not be large relative to the income the worker expects over the rest of his lifetime, and may not result in reduced work effort. For example, if a worker age 64 is trying to decide whether to retire completely at age 65 or to work one more year and then retire, the lump sum of, say, $8,000 in restored benefits due to repeal of the earnings test would add only a small amount of income each year when spread over, say, a sixteen year retirement, ages 66 through 81. The increase in the retiree's annual income would really be only the interest on the $8,000, plus a bit of the principal.

-- Second, for workers who plan to continue working until age 75 or 80, well past age 70 when the earnings test no longer applies, the lump sum loss of benefits for the intervening years is a nuisance but not a strong deterrent to retaining one's job. Thus, restoration of lost benefits from repeal of the earnings limitation would not trigger a drop in work effort.

Estimating behavior and revenues.

It should be noted that any revenue estimates on the tax consequences of eliminating the earnings test prepared by the Joint Tax Committee, the Congressional Budget Office, or Treasury will likely include only the revenue from the direct taxation of the added benefits paid. The estimates will be unlikely to include any revenues due to higher employment and earnings of the elderly as a result of the repeal. Each agency as a matter of policy sticks to an unchanged economic baseline forecast in performing revenue estimates. Real world changes in GNP and associated revenue changes due to a policy shift are ignored.

The rationale behind this "static" estimation technique is three-fold. First, there is no consensus in the economics profession on the precise means by which taxes and transfers affect behavior; while it is known that some policy changes are more likely to alter behavior than others, the absolute and relative magnitudes are not agreed upon. Second, "dynamic" revenue estimation is of course more work. And third, there is concern that, in the absence of precise agreement as to rules of determining behavior changes and revenue reflows, interest groups and bill sponsors might have even more incentive than at present to make exaggerated claims for their favorite legislation.

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[1] See Gordon and Schoeplein, "Tax Impact From Elimination of the Retirement Test", Social Security Bulletin, September 1979/Vol. 42, No.9.

The one certainty in all this is that the effect of a policy change is not zero. While no revenue reflow estimate will ever be perfect, the assumption of zero reflow is bound to be incorrect, and acts to exaggerate the cost of pro-growth policy changes.

Failure of the revenue estimators to adjust receipts for changes in the economy would create an even greater problem if one were to consider repeal of the earnings test for persons age 62 through 64, where continuation of previous full time employment at higher wages is more likely than at an older age. It would also matter more in consideration of other tax changes on the working age population and in the tax treatment of capital in an open world economy, where behavior shifts and revenue reflows can be substantial. Capital gains is a case in point.

Repeal of the earnings test.

Repeal of the earnings test is most often discussed for ages 65 through 69, where complete repeal would cost about $5 billion per year in higher outlays, before offsets. As mentioned above, about ten percent of this cost might be recovered through taxation of benefits and higher income and payroll taxes due to higher earnings under the most conservative assumptions, and over half the cost under more likely assumptions.

Minor adjustments to the benefit computation process that have been considered at one time or another by SSA and the Congress might be employed to provide additional savings. For example, accelerating the increase in the delayed retirement credit to 8 percent in 1989 would encourage later retirement, and save about $0.4 to $0.5 billion per year. Eliminating the recomputation of benefits for additional earnings after reaching normal retirement age could save about $0.8 billion per year. Elimination of the excess earnings exception to the rule on retroactive entitlement in reduced benefit cases would save about $0.2 billion per year. Administrative cost savings of nearly $0.1 billion should be counted as well.

These offsets and tax reflows would cover a significant portion of the cost of repeal. In addition, a phase-in of the reform could make the task even easier. For example, assuming no offsets or tax reflows, eliminating the test for those age 69 in 1989, age 68 in 1990, and so on would cost under $1 billion the first year, rising in stages to the full $5 billion in 1993. During this period, normal real economic growth will be raising real Federal revenues by about $30 billion each year, or by over $150 billion annually by 1993. To implement this reform would take only a bit over 3 percent of the real growth of revenues over five years, even without offsets and measured on a purely static basis.

Consideration should also be given to eliminating the earnings test for those below normal retirement age. There would be more recovery of costs from added work effort and tax payments from this group. This would increase the cost of repeal, but a phase-in could cushion the impact. Perhaps the early retirement penalty could be adjusted slightly to defer part of the cost. However, this should not be done without considerable advance notice to give people time to save or to plan to work an additional few months to make up for the change in the benefit computation procedure. Finally, some consideration could be given to a small adjustment to the benefit formula itself, effective some years from now. As shown in the attached table, the current formula provides for very large increases in real benefits per retiree in the years ahead. Perhaps a trade-off could be devised of a reduction in the outyear replacement rates and the projected benefit increases for a phase-out of the earnings test for the lower age group.

Incidence of the reform.

Much will undoubtedly be made over the distribution across income classes of added benefit payments under repeal of the earnings test. For those aged 65 through 69, a bit under half of the cost would come from raising the ceiling to $25,000, and a bit over half from lifting the ceiling entirely. This is not the way to view the proposal for several reasons:

-- No taxpayer should have to face tax rates of 65 to 85 percent, let alone rates over 100 percent. The latter are virtually federal orders of forced retirement. Even a 65 percent rate is contrary to the spirit of tax reform.

-- Progressivity should be addresed in the basic structure of exemptions and tax rates, not piecemeal in obscure corners of the tax code and entitlement programs. No one devising a new tax code and income transfer system would handle the problem with a peculiar penalty on persons age 62 to 69.

-- While repeal may send additional benefits to upper income persons, they are likely to be taxed on those benefits to a greater degree than others who benefit from repeal.

-- There are already too many peculiar "spikes" in the tax and entitlement programs, including rapid loss of welfare benefits as earnings rise, the sharp phase-out of the earned income tax credit, phase-in of social security benefit taxation, the tax-based premium surcharge for catastrophic coverage in Medicare, and the 5 percent surcharge eliminating the 15 percent bracket and the personal exemption for upper income taxpayers, resulting in a 33 percent federal income tax rate for those affected.

Conclusion

It would be extremely beneficial from an economic, tax simplification, administrative, and personal liberty standpoint to repeal the social security earnings test. Budget and distributional concerns are minor by comparison with the benefits to be had from this reform, and can be dealt with via phased reductions and other adjustments to the benefit computation rules.

Table

Projected Initial Real Benefits for Single Retirees
Age 65 with Average and Maximum Covered Earnings (Alternative II-B)

Retirement Year	Annual Benefits: Current Dollars Average	Current Dollars Maximum	Constant 1988 Dollars Average	Constant 1988 Dollars Maximum	Replacement Rate Average	Replacement Rate Maximum
1988	7,534	10,095	7,534	10,095	42.2	23.0
1990	8,621	11,690	7,905	10,719	44.0	25.1
1995	10,558	14,691	7,941	11,050	41.4	24.4
2000	13,762	19,891	8,508	12,297	41.4	25.3
2005	17,907	26,827	9,099	13,632	41.4	26.2
2010	23,291	35,931	9,727	15,006	41.4	27.1
2015	30,297	47,635	10,400	16,352	41.4	27.6
2020	39,415	62,214	11,121	17,553	41.4	27.7
2025	51,277	80,942	11,891	18,771	41.5	27.7
2030	66,704	105,292	12,714	20,069	41.5	27.7
2035	86,769	136,776	13,594	21,428	41.5	27.7
2040	112,866	177,910	14,534	22,909	41.5	27.7
2045	146,811	231,374	15,538	24,488	41.5	27.7
2050	190,964	300,899	16,612	26,175	41.5	27.7
2055	248,410	391,411	17,761	27,986	41.5	27.7
2060	323,127	509,142	18,989	29,921	41.5	27.7
2065	420,320	662,284	20,303	31,990	41.5	27.7

Assumes retirement at age 65. Beneficiaries are assumed to have been full time workers earning the average wage in covered employment, or the maximum covered wage throughout their working lives. Married couples with a spousal benefit would receive 150 percent of the amounts shown in the table. Data were provided by the Social Security Administration.

STATEMENT OF WAYNE VROMAN, SENIOR RESEARCH ASSOCIATE, THE URBAN INSTITUTE

Mr. VROMAN. Thank you.

I am here as an employee of the Urban Institute, but I worked a couple years at the Social Security Administration, and at that job one project I worked on was the retirement test, and recently I have had occasion to do a second study of the retirement test. I am happy to be here today. I have fairly strong opinions about it.

To pick up a theme Mr. Daub raised earlier, it is interesting to look at the retirement test from a historical perspective because the test has evolved a great deal in the last 30 years. Let me illustrate this in three areas. The age at which people are exempt from the retirement test, initially it applied to all people over 65. It was lowered to 75 in 1950, to 72 in 1955, to 70 in 1983, so the oldest of the aged are now completely exempt from the program.

The amount that a person can earn and still collect benefits has been substantially liberalized over the course of the program partly by changing the exempt amount and partly by changing the benefit reduction rate. When the retirement test was first put in place, benefit reduction rates when earnings exceeded a threshold initially were set at 100 percent. In 1961, a benefit reduction rate of 50 percent was put in place and then at a second higher level the rate of 100 percent was still in place.

In 1972, the 100 percent benefit reduction point was completely eliminated, and that has persisted down to the present. From 1973 to the present, the benefit reduction rate has been 50 percent. That is scheduled to decline to 33 percent in 1989. So there has been substantial liberalization of the retirement test in the last 20 years.

Maybe it would be worth emphasizing how much change has taken place in the real value of the exempt amount in the last 12 years. In 1977, a Social Security amendment substantially raised the annual exempt amount from $3,000 in 1977 to $4,000 in 1978, and then by $500 increments in the succeeding 4 years. If you think about an older person in the age group affected by the retirement test working at average hourly earnings, in 1977 the person could have worked 571 hours and not lose any benefits. By this year, the person could have worked 900 hours and not have lost any benefits. So the real value of the exempt amount measured relative to average earnings in the economy has gone up about 60 percent over the last 12 years.

Since the program is indexed, there is likelihood there will be no erosion of that exempt amount. I think you can make an argument for further raising the exempt amount, and I will return to that later.

A major trend that is obvious to anyone who talks about retirement in our economy is how much less people of older ages work now compared to 10, 20 and 30 years ago. I have an exhibit in my written statement showing men aged 65 to 69, how much they work now and going back all the way to 1955. And the trends are really startling. Men working full time full year used to account for about 40 percent of the men in this age group. Now they account for about 13 percent. Men who used to work full time at jobs between 27 and 49 weeks per year used to represent about 10 per-

cent of this age group; now they represent about 3 percent. So you had almost a 33 percentage point reduction in men working, the largest amount in this age group, and that has been matched not by increases in part-time work but by people who don't work at all.

In 1955, men who didn't work at all were about 32 percent of the total; now they are 60 percent of the total. If you look at what the elderly are actually doing, they are voting with their feet, getting out of the labor force, and they have been doing this in the last 10 years when the retirement test has been moving in a direction which would let them work more. Early retirement provisions are impacting people in their 50's. People have enough combined income from pensions, savings and other sources so that they are able to go into retirement in their preferred mode of retirement, which in many instances is not to work at all. That shows up in the data again and again.

I had a chance to examine beneficiary earnings, that is social security beneficiary earnings, in the 1970's. Three things were obvious involving people subject to the test. The proportion who worked at all dropped substantially from 31 percent of beneficiaries in 1970 to 17 percent in 1980. In each year, the proportion who worked and earned an amount that was right near the annual exempt amount caused a noticeable bulge in the earnings distribution, but over the decades of the 1970's, the loading of people at that point declined very substantially. At the start of the decade, over 5 percent of the beneficiaries earned right around $1,680, which was the exempt amount. By the end of the decade, 1.1 percent earned near $5,000.

The other trend in the 1970's was people earning above the exempt amount became less numerous. There was no major increase in proportion of beneficiaries earning less than the exempt amount. I estimated the labor supply for the typical beneficiaries went down by about 50 percent mainly through complete absence from the labor force compared to the start of the decade.

Now it is obvious that the presence of the retirement test causes a limitation in income. For certain people you can't have your full benefits and you can't earn as much as you want when you are age 65 to 69.

The study also had an opportunity to look at the income characteristics and effects that it might have on poverty if the retirement test were changed. My study there found that the main loading of poor people age 65 to 71 in the population was people who didn't work at all. So if the retirement test is to have an effect on poverty, the very lowest income segment of the aged population, it is going to have to induce people to come back into the labor force and start working. I know of no evidence to suggest there have been major changes that would induce people to do that. The biggest changes in the exempt amount that took place in 1973 and 1978.

When you look at beneficiaries subject to the test and the portion who worked, there is no noticeable change in the proportion who worked. In 1983, we had a major change in the age of exemption from the retirement test. If people really thought there was a major disincentive effect, why hasn't someone done a study showing the number of 70- and 71-year-olds who moved back into the labor force because they have been exempt from the retirement

test since 1983? I submit to you that study hasn't been done because there has been no change in labor supply behavior for elderly beneficiaries of that age group. People go out of the labor force, and they stay out. That is the fact.

As far as policy options, one could think about doing one of three things: raise the exempt amount, reduce the benefit reduction rate, or eliminate the test altogether. Currently the $8,400 exempt amount, if someone is making average hourly earnings, represents 900 hours a year of work. If you thought an elderly person should have a legitimate shot at working half a normal 40 hours a week for the full year, that would imply a retirement test if they were making average hourly earnings of $9,700. You could be more generous and say let's move it up to three-quarters of a year, 1,560 hours that would imply a test of $14,500 for this year.

For people who are making average earnings and less, one could make substantial liberalizations in the retirement test that would affect their hours of work without raising the exempt amount that much, and that would be a much less costly program for the Social Security trust fund than $20,000, $25,000 or a total elimination of the test.

Congressman Daub, I think I have fairly strong disagreements with you about the amount that labor supply has really been held down by the test. It has basically been liberalized, and yet older people on average are working less than they did 10, 20, 30 years ago.

Thank you.

[The statement of Wayne Vroman follows:]

THE SOCIAL SECURITY RETIREMENT TEST

Statement before the
Subcommittee on Social Security
of the
Committee on Ways and Means,
U.S. House of Representatives

by

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September 29, 1988

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The views expressed in this statement are those of the author and do not necessarily represent the views of The Urban Institute or its sponsors.

I would like to thank the subcommittee on Social Security for the opportunity to share some observations regarding the Social Security retirement test. I am a former employee of the Social Security Administration, Office of Research and Statistics, and have conducted two studies on the effects of the retirement test. Some of the comments and supporting material will be based on these earlier studies. My testimony will focus on five areas: (1) the evolution of the retirement test, (2) trends in work habits of men aged 65-69, (3) the earnings patterns of beneficiaries subject to the retirement test, (4) the link between the retirement test and poverty and (5) potential changes in the retirement test. My main recommendations would be (1) to retain the retirement test and (2) to raise the annual exempt amount.

The Evolution of the Retirement Test

Social Security beneficiaries younger than age 70 can receive full annual benefits only if their earnings do not exceed a level specified by the program's earnings test. The earnings test, also commonly referred to as the retirement test, is intended to limit the joint amount of OASI benefits and labor market earnings among beneficiaries. Although its specific provisions have undergone several changes since the 1930s, the test's intent has been constant: to limit benefits among those who exhibit substantial continued labor market activity. Persons who are retired would not be expected to have high earnings and the test provides an operational way to define retirement.

Originally the earnings test focused on the monthly earnings of beneficiaries regardless of age. Before 1950 benefits were completely withheld in any month that the beneficiary earned $15 or more. People aged 75 and older were exempted from the test starting in 1950 and the permissible amounts of monthly earnings were raised to $50 and $75 in 1950 and 1952 respectively. Since 1955 the test has focused primarily on annual earnings and has applied only to beneficiaries younger than age 72 (age 70 since 1983). Thus one could earn $1,200 in 1955 in any monthly pattern without a loss of benefits. If earnings exceeded $1,200, however, a full month of benefits would be withheld for each $80 (or fraction of $80) in excess of $1,200. The earnings limit below which full annual benefits are received, $1,200 in 1955, is termed the annual exempt amount. Table 1 shows the annual exempt amount for selected years between 1955 and 1988. Although annual earnings were of primary importance there continued to be a monthly test in 1955 and later years. One could receive full monthly benefits for any month in 1955 when earnings fell below $80 even if annual earnings were substantially above $1,200.

Starting in 1961 annual earnings between $1,201 and $1,500 caused only a $.50 benefit reduction for each extra dollar of earnings. In this range the earnings test had an effective "tax" rate; i.e., benefit reduction rate, of 50 percent. A 100 percent effective tax rate was then applied to earnings above $1,500. This 100 percent benefit reduction point was then raised to $1,700 in 1962. Subsequent legislation that became effective in 1966 and 1968 further raised both the 50 percent and 100 percent benefit reduction points and they stood at $1,680 and $2,880 respectively from 1968 to 1972.

Legislation enacted in 1972 eliminated the 100 percent benefit reduction point (effective in 1973), raised the annual exempt amount substantially (to $2,100) and provided for indexing the exempt amount based on increases in average wages in covered employment (effective in 1975). Due to indexing, the exempt amount increased annually and by 1977 it had reached $3,000. Thus a beneficiary could earn up to $3,000 without loss of benefits and higher earnings were subject to a 50 percent benefit reduction rate until all benefits were withheld. The permissible earnings amount under the monthly test had risen to $250 by 1977. Later we will focus on earnings and poverty status of persons subject to the retirement test in 1977.

The Social Security Amendments of 1977 made important changes in the retirement test. (1) The annual exempt amount for workers aged 65 to 71 was raised to $4,000 in 1978 and by $500 increments in successive years until it reached $6,000 in 1982. Thereafter, it was scheduled to rise automatically with the average level of covered earnings. (2) Starting in 1982 the age at which beneficiaries are exempted from the retirement test was to be lowered from 72 to 70. The actual implementation of this provision was delayed until 1983. (3) The monthly test was abolished except for the year of initial entry into beneficiary status. This modification was designed to reduce benefits among workers with highly seasonal earnings who could collect benefits in some months because their annual earnings were concentrated in the remaining months of the year. Previously such persons could collect benefits even thought they were not retired and had substantial annual earnings. (4) The change in the 1978 annual exempt amount to $4,000 was not extended to workers

younger than age 65. Their exempt amount continued to be indexed but rose only to $3,240 in 1978. Younger beneficiaries have been subject to a lower exempt amount in all years since 1978. Table 1 shows that by 1982 the differential had reached $1,800; i.e., $5,160 versus $6,960. By 1988 the differential had reached $2,280 ($6,120 versus $8,400). Since both exempt amounts are indexed to average covered wages, this proportional differential of 26 percent under present law will persist in future years.

The 1977 amendments caused a substantial upward revision in the annual exempt amount for 65-71 year olds. To give an idea of the real increase the final columns of Table 1 display average hourly earnings and the number of annual hours that are represented by the exempt amount. For a worker paid the average hourly wage rate the table shows the number of hours that could be worked by someone who wanted to collect their full annual benefit entitlement. Since actual hourly earnings vary widely, these estimated hours should be viewed as representative of a "typical" working beneficiary and not applicable to everyone. Changes in the estimated hours, however, illustrate how the liberality of the earnings test changed in these years. For beneficiaries aged 65 to 69 annual work permitted by the exempt amount (at the average hourly rate of pay) increased from 566 in 1974 (571 in 1977) to 901 in 1988 or by almost 60 percent.

Between 1955 and 1977 when a common exempt amount applied to beneficiaries of all ages, the number of annual work hours permitted by the test (at the average wage rate) varied from a high of 702 in 1955 to a low of 454 in 1972. For most of these twenty-three years the number of permissible work hours varied between 500 and 600. Since 1977, however, there has been a major liberalization in the annual exempt amount. The 901 hours indicated in Table 1 for 1988 represents 43 percent of the 2080 annual hours of a person employed forty hours per week for all fifty-two weeks. Work incentives provided by the retirement test will further increase in 1990 when the benefit reduction rate (or implied tax rate) for earnings in excess of the annual exempt amount declines from 50 percent to 33 percent.

Work Habits of Men Aged 65-69

The trend towards reduced labor force attachment among the elderly is well known. Table 2 presents summary data on the work experiences of men aged 65-69 over the years when the retirement test has had an annual exempt amount, i.e. since 1955. For men who worked sometime during the year, six categories of annual work experiences are shown (by the number of weeks and by full-time or part-time status). Three major trends in the work experience proportions are seen: downtrends in full time work of 50-52 and 27-49 weeks and a major uptrend in the proportion not working at all during the year (from .318 in 1955 to .658 in 1987). No major trends are observed in the part-time work categories which show increases between 1955 and 1969 but decreases after 1969. Despite liberalizations in hours of work permitted by the retirement test since 1977 part-time work has actually become somewhat less prevalent among men in this age group.

When asked why they do not work, men aged 65-69 usually respond that they are retired or have a health condition that precludes work. Very few indicate their nonwork status is the result of being unable to find a job. Since being retired or disabled usually results in receipt of Social Security benefits the next section discusses a study of beneficiary earnings patterns.

Social Security Beneficiary Earnings: 1970 to 1980

During the 1970s the retirement test underwent several significant modifications as discussed previously and partially summarized in Table 1. Three important changes were (1) large increases in the annual exempt amount (L), which increased from $1680 in 1970 to $5000 in 1980 for beneficiaries aged 65-71, (2) abolition of the second break point in the test after 1972 where higher earnings caused benefits to be reduced on a dollar-for-dollar basis and (3) restrictions in the scope of the monthly test after 1977.

This section which summarizes annual distributions of earnings for beneficiaries aged 65 to 71 reports results from a larger study of the earnings of old-age, survivor and disability beneficiaries.[1] The data set for the investigations was assembled using merged records from the Census Bureau's March 1978 Current Population Survey (CPS) and program data from the Social Security Administration (SSA). The latter included both annual taxable earnings from the Summary Earnings Record (SER) and selected beneficiary data from the Master

[1]Wayne Vroman, "Some Economic Effects of the Social Security Retirement Test," Research in Labor Economics, Volume 7 (1985), pp 31-89.

Beneficiary Record (MBR). To ensure that strict confidentiality of individual microrecords was maintained, the merged data file was assembled under the supervision of the Internal Revenue Service. The file combines CPS information on family income in 1977, various socioeconomic and demographic characteristics as of March 1978, along with SSA program data on covered earnings and benefits.

Table 3 displays earnings distributions for (old age and survivor) beneficiaries aged 65 to 71 for the eleven year period from 1970 to 1980. Each person in the table was already in benefit status on January 1 of the indicated years. Since new entrants into benefit status were excluded from the tabulations in their first year of receiving benefits, cases of very high annual earnings do not reflect current year retirements. The earnings intervals in Table 3 were selected to highlight beneficiary responses to changes in the annual exempt amount. For each year the exempt amount is bracketed by a $200 or $300 interval and the relevant interval is identified (with a superscript L) for all eleven years.

It is obvious in Table 3 that the retirement test has important effects on beneficiary earnings. First, notice that most beneficiaries have no earnings. The nonworker proportion ranged from a low of .694 in 1970 to .829 in 1980. Most of the increase in the nonworker proportion occurred in the first half of the 1970s.

The table also clearly shows that the annual exempt amount has an important effect on the earnings of beneficiaries who continue to work. The 152 persons in the exempt amount interval in 1970 represent 5.7 percent of all beneficiaries. In every other year the exempt amount interval also has a large concentration of beneficiaries. Between 1970 and 1980, however, both the number and the proportions in the exempt amount interval declined. The 55 person in the $4901-$5100 interval in 1980 represented 1.1 percent of all beneficiaries or about one-fifth of the corresponding proportion of ten years earlier.

Earlier in Table 1 it was noted that changes in the annual exempt amount applicable to 65-71 year olds exceeded changes in the general level of wages after 1977. The exempt amount represented 520 hours of work at the average wage in 1970, 571 hours in 1977 and then 751 hours in 1980, an increase of 32 percent over the 1977 level. The large post-1977 increases in the potential work hours might be expected to reduce the numbers in the exempt amount interval. Many working beneficiaries would find it difficult to rearrange part time and/or part year work schedules in order to fully adjust their annual earnings to the higher permissible amounts. Table 3 does show lower proportions earnings near the exempt amount in 1978-80 when compared to 1977. What is more striking about these proportions are the declines that occurred earlier in the decade; i.e., from 0.57 in 1970 to .023 in 1977. This earlier decline occurred in a period when the normalized annual exempt amount (the amount divided by average hourly earnings) was nearly constant. Thus most of the 1970-to-1980 decline in this proportion predated the large increases in the annual exempt amount that occurred after 1977.

Periodic increases in the annual exempt amount as occurred in the 1970s might exceed the amounts by which some older workers could raise their earnings (and still collect their full annual benefit entitlement). In this situation, decreases in the proportion earning near the exempt amount could occur while the proportion in the rest of the interval below the exempt amount would increase. Table 3 shows that this phenomenon was not a major trend during the 1970s. The proportion with some earnings but less than $1,501 (the lower limit of the exempt amount interval) was .137 in 1970. The corresponding proportions in later years ranged from .124 to .155. These proportions clearly did increase in 1973 and 1978, the years between 1970 and 1980 when the real increases in the exempt amount were the largest. Both increases were then followed by declines in subsequent years, i.e. 1975 and 1980 respectively, even though the real value of the exempt amount did not decline. As a consequence, for the decade as a whole there was no noticeable increase in the proportion with earnings in the entire interval below the exempt amount.

The other striking feature in Table 3 is the large number of beneficiaries with high earnings in the early 1970s. The 297 beneficiaries with earnings above the exempt amount interval in 1970 ($1801 and above) and the 46 with earnings above $7000 represent 11.2 and 3.6 percent respectively of all beneficiaries. After 1970 there are sharp falloffs in the numbers of high earners so that the corresponding 1974 percentages are 4.3 and .9 percent respectively. Note that in all years there are comparatively few beneficiaries who earned just above the annual exempt amount, i.e. in the range where the retirement test has a 50 percent benefit reduction rate. Finally, although the total number of beneficiaries in Table 3 nearly doubled between 1970 and 1980, there were more persons with earnings above $7000 in 1970 (96) than in 1978-80 (49, 64 and 72 for the latter years, respectively). Because nearly all of this decline occurred early in the decade, it cannot be attributed to the revised provisions of the monthly retirement test that became effective in 1978.

During the 1970s the average earnings of working beneficiaries aged 65-71 increased, but much less rapidly than the amounts permitted by the periodic revisions in the annual exempt amount. The 1970 earnings mean of $2,449 was 146 percent of the exempt amount while the 1977 and 1980 means of $2,532 and $3,451 were only 84 and 69 percent respectively of the exempt amounts for these years. From Table 3 it is clear that two factors account for the low growth in mean earnings, decreases in the numbers with annual earnings above the exempt amount and decreases in those with earnings in the exempt amount interval. Because beneficiaries with high annual earnings became less common in the 1970s, mean earnings grew much more slowly than did the annual exempt amount.

In summary, four observations about 65-71 year olds are as follows. (1) The majority do not work. (2) Those who work respond to changes in the annual exempt amount. (3) During the 1970s the concentration of beneficiaries with earnings near the annual exempt amount declined sharply. (4) There is evidence of labor supply reductions between 1970 and 1980.

What is especially striking is the extent of the labor supply reductions among beneficiaries aged 65-71. The proportion with covered earnings during the year declined from .306 in 1970 to .171 in 1980 or almost by half of its 1970 level. Among those who worked mean earnings grew from $2,449 to $3,451 or by 41 percent. Compared to the 106 percent growth in average hourly earnings (from $3.23 in 1970 to $6.66 in 1980), this low rate of average earnings growth suggests that during the 1970s there were sizeable labor supply reductions among working beneficiaries. Considering both the decline in the proportion who worked and the low growth of mean earnings among working beneficiaries, it is clear that per capita labor supply in this age group declined by more than half between 1970 and 1980.

The observed decline in labor supply occurred despite a substantial liberalization in the retirement test's annual exempt amount. A worker paid at the average hourly wage rate and subject to the test could work about 50 percent more hours in 1980 than in 1970 and still collect full annual OASDHI benefits. Despite upward revisions in the exempt amount that would encourage increased labor supply, actual labor supply moved strongly downward. The decreased labor supply is probably explained by a combination of factors including an increased taste for leisure, an income effect caused by higher OASDHI and other retirement benefits and a decline in the demand for older workers. Whatever the full explanation, it is clear that beneficiaries aged 65-71 worked much less at the end of the decade than they did in 1970

The Retirement Test and Poverty

The data just examined and other research have demonstrated that beneficiaries subject to the retirement test are influenced by the test's annual exempt amount. Since earnings and OASDI benefits are the two largest income sources for many older persons and their families, the presence of the retirement test could affect occurrences of poverty in the elderly population. For some persons aged 65-69 the retirement test limits their earnings or the size of their OASI benefits. If the test were either substantially liberalized or abolished it would allow these persons to increase their income. In some instances the additional income would be sufficient to raise these individuals and their families out of poverty.

The 1978 CPS-SER-MBR data base discussed earlier allows one to directly examine the link between earnings and poverty status of OASI beneficiaries in 1977 (the CPS income year for the data base). Table 4 provides summary information on earnings and poverty status of beneficiaries and nonbeneficiaries aged 65 to 71 in 1977. There were 3859 beneficiaries and 639 nonbeneficiaries aged 65-71 in the data base. The annual exempt amount in 1977, $3000, is bracketed by the $2601-3300 earnings interval. Of the 3859 beneficiaries 171 or 4.4 percent had earnings in this interval. An additional 415 (or 10.8 percent) earned less than $2601, 117 earned more than $3300 while 3156 (or 81.8 percent) had no earnings during 1977.

Overall, 11.8 percent of the OASI beneficiaries lived in poverty, a poverty rate nearly identical to the 11.6 percent rate applicable to the entire U.S. population in 1977. When the earnings status of these beneficiaries is examined it becomes clear that poverty is concentrated among nonworkers. Of the 3156 nonworkers, 407 were poor in 1977 for a poverty rate of 12.9 percent. Thus nonworkers accounted for 81.8 percent of beneficiaries in these data (3156 of 3859) but 89.5 percent of poor beneficiaries (407 of the 455 in poverty). Those with earnings above $1500 have low poverty rates.

From Table 4 it is clear that poverty among OASI beneficiaries is concentrated in the nonworking segment of the beneficiary population. If modifications in the retirement test are to affect this group, they would have to reenter the labor force. Many have not worked for several years and a large segment have physical

disabilities and other health conditions that would make even part-time work an unlikely option. Since more than 80 percent of beneficiaries are nonworkers, however, inducing some to return to work would raise their income and could reduce their poverty rates. From Table 4 it is clear that most nonworkers (87 percent) are not poor. Even if some segment of nonworkers could be induced to work through a change in the retirement test there is no guarantee that it would be the low-income segment.

Critics of the retirement test often advocate its abolition. Two certain consequences of its abolition would be to increase the number of program beneficiaries and to increase the total amount of benefit payments. In the short run at least the effect of abolishing the retirement test would be to lower the OASI trust fund balance. The exact affect on the trust fund is not known with certainty since there are labor supply effects that need to be considered.

Abolishing the retirement test would also have income distribution effects that should be emphasized. The 1978 CPS-SER-MBR exact match file from my earlier project did not identify all eligible nonbeneficiaries. Because the file was longitudinal, however, it did identify an important subset of this group, i.e. 1977 nonbeneficiaries who entered benefit status sometime during the next three years. The last three columns of Table 4 show counts and poverty rates for persons who delayed their entry into benefit status until they were at least 66 years old. Since persons aged 72 and older in 1977 were not subject to the earnings test, the interesting members of the delayed retiree group are the 66-71 year olds. Note that men and women in this group are distinguished in Table 4. All of the men became old age beneficiaries after 1977 while the women became both old age and spouse beneficiaries.

As a group the delayed retirees aged 66-71 had high earnings and low poverty rates in 1977. While 18.2 percent of beneficiaries and 37.5 percent of nonbeneficiaries had covered earnings in 1977, 78.3 percent (112 of 143) of the delayed retirees were active workers. Further, of the 112 active workers, 98 earned more than $6,000 in 1977 and had a poverty rate of 1.0 percent for the year. The group had an overall poverty rate of 5.6 percent, half the rate for beneficiaries and one-third the rate for all nonbeneficiaries of the same age. Female poverty rates are much higher than male rates in this group, 10.7 versus 2.3 percent, reflecting the presence of subsequent spouse beneficiaries as well as old age beneficiaries.

Another relevant way to describe the delayed retirees is to compare them with 1977 nonbeneficiaries aged 65-71 who did not retire in the next three years. The two groups combine to form the nonbeneficiary total (638 persons) in Table 4. The delayed retirees have a 1977 poverty rate of 5.6 percent while the (495) others have a poverty rate of 19.6 percent. Considering that this latter group has an unknown number of OASI-eligibles who still had not retired by the end of 1980, it is clear that those who delayed retirement are very well off while those who remain nonbeneficiaries (primarily because of ineligibility) are quite a poor group of older persons.

These findings have direct relevance for proposals to abolish the retirement test. Abolition would raise the income of eligible nonbeneficiaries. As a group, however, these persons have high earnings and high income. They do not collect benefits because the opportunity cost imposed by the retirement test, i.e. forgone earnings, is too high. There are poor nonbeneficiaries aged 65-71. Most of these persons do not work, are not eligible for OASI benefits, and would not be helped by an abolition of the retirement test.

Summary and Potential Changes

From the data examined earlier it was clear that OASI beneficiaries are knowledgeable about the retirement test and that its provisions influence beneficiary earnings. Table 3 shows that after 1972 when the annual exempt amount changed each year, the distribution of earnings shifted upward and there always was a concentration of beneficiaries with earnings near the exempt amount. For beneficiaries aged 65-71 there were especially large increases in the exempt amount after 1977. Even before that year, however, it was clear that the exempt amount was increasing more rapidly than average beneficiary earnings. Among those with earnings the ratio of mean earnings to the exempt amount decreased from 1.46 in 1970 to .84 in 1977. By 1980 the ratio had fallen to .69. Thus during the 1970s upward revisions in the annual exempt amount exceeded the ability (and/or desire) of these persons to increase their annual earnings. Indicative of their situation, the proportion with earnings in the exempt amount interval (Table 3) fell from .057 of beneficiaries aged 65-71 in 1970 to .023 in 1977 and to .011 in 1980. For the group as a whole upward revisions of annual earnings during the 1970s were not seriously impeded by the provisions of the retirement test.

During the 1970s there was a sizeable reduction in the proportion of beneficiaries aged 65 to 71 who had any earnings during the year (from .306 in 1970 to .171 in 1980). This was associated with reductions in the proportion with earnings near the annual exempt amount and the proportion with earnings above the exempt amount. Combined, these changes suggest there were major reductions in the labor supply in a period when the exempt amount evolved so as to permit increased annual work hours among beneficiaries aged 65 to 71.

Although some beneficiaries limit their earnings because of the earnings test, the test is not an important cause for poverty in the aged population. Most of the aged poor have no earnings at all. Those with earnings near the annual exempt amount had a poverty rate of only 5.7 percent in 1977, about half the rate for all OASI beneficiaries aged 65-71. Since nearly 90 percent of poor beneficiaries had no earnings at all, revisions in the earnings test would not be expected to affect them or to affect overall poverty rates in the beneficiary population. Only if sizeable numbers of nonworkers were attracted back into the labor force could a change in the test have a sizeable impact on poverty rates. There is very little likelihood that such behavior would be expected to occur.

For beneficiaries aged 65-71 the earnings test has been liberalized substantially since 1977. The increase in the annual exempt amount from $3,000 in 1977 to $8,400 in 1988 represents a 58 percent increase in potential annual hours from 571 to 901 when measured relative to average hourly earnings in the private nonfarm economy. Mean earnings of working beneficiaries have certainly grown more slowly than the growth in the exempt amount. In order to permit even higher beneficiary earnings without any loss of benefits one could set the exempt amount so as to permit 1040 annual hours (at the average hourly wage) or half time work by aged beneficiaries. In 1988 this amount would have been $9,700, about 15 percent more than the actual exempt amount of $8,400. An even more substantial increse to $14,500 would permit 1540 annual hours of work or three quarters of a full-time full-year work schedule. Such increases would permit some beneficiaries to have considerably higher earnings without any loss of benefits. At the same time, however, the higher exempt amount would still prevent those with very high earnings from collecting benefits.

A second way to liberalize the earnings test would be to lower the benefit reduction rate applicabale to those with earnings above the annual exempt amount. Currently the benefit reduction rate is 50 percent, but for those aged 65 to 69 it is scheduled to be reduced to 33 percent in 1990. This too will permit some individuals to achieve a higher income (by a higher combined sum of earnings plus benefits) than is now attainable. From the data examined in Table 3, however, two comments should be made. First, not many beneficiaries had earnings in the 50 percent benefit reduction range during the 1970s. Second, to the extent that persons earning near the annual exempt amount would be the ones to raise their earnings, the large decline in the size of this group during the 1970s has greatly diminished the potential aggregate importance of this beneficiary response. Recall that the proportion of 65-71 year olds with earnings near the exempt amount fell from .057 in 1970 to .011 in 1980. Thus it would appear that the lower benefit reduction rate will not affect many beneficiaries when it becomes applicable in 1990.

A third policy option is to abolish the earnings test. If implemented this certainly would permit some beneficiaries to increase their earnings and their income. Also, the beneficiary population would increase as eligible nonbeneficiaries would enter benefit status. From material examined in Table 4, however, it is also clear that eligible nonbeneficiaries already have very high incomes so that the aged poor would not gain from this potential policy action. Even if abolition of the retirement test did cause nonworkers to reenter the labor force, there is no guarantee that poor beneficiaries would be the ones to exhibit this behavior. Thus, if one wanted to reduce poverty rates in the aged population, abolition of the earnings test would not be an effective policy action.

To summarize, increasing the exempt amount and lowering the benefit reduction rate are two policy actions that would permit some older beneficiaries to raise their incomes. These actions would allow a higher combined sum of earnings and OASI benefits. Those helped by such changes, however, would not be the aged poor, but persons with incomes of one to two times the poverty line and higher. Outright abolition of the test, on the other hand, would mainly benefit an even higher income group of aged persons. From the standpoint of social adequacy it would seem preferable to liberalize rather than abolish the OASI retirement test.

Table 3. The Annual Earnings of Beneficiaries Aged 65-71: 1970 to 1980[a/]

Annual Earnings	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
	Beneficiary Counts										
0	1842	2123	2327	2515	2724	3054	3284	3514	3720	3857	4154
1-500	105	141	131	135	123	105	103	101	117	103	93
501-1000	133	117	93	110	104	92	94	103	88	97	85
1001-1500	125	117	135	115	102	100	91	79	64	72	68
1501-1800	152[L]	150[L]	155[L]	69	74	64	44	56	48	52	39
1801-2000	29	22	21	51	40	41	40	33	35	39	30
2001-2300	25	23	24	101[L]	82	67	46	57	44	50	46
2301-2600	22	9	12	28	91[L]	122[L]	80	69	50	36	36
2601-2900	11	6	10	10	18	29	129[L]	76	47	53	34
2901-3100	7	4	5	5	13	13	17	101[L]	53	32	19
3101-3300	7	6	4	7	4	5	15	17	31	29	19
3301-3600	9	3	4	11	6	7	8	19	30	44	51
3601-3900	9	5	15	3	6	10	6	14	56	45	39
3901-4100	5	3	1	1	6	3	6	6	64[L]	35	21
4101-4400	9	4	4	5	5	3	9	10	27	58	33
4401-4600	4	5	3	2	3	2	4	6	14	82[L]	18
4601-4900	13	7	6	2	4	3	4	3	5	19	38
4901-5100	7	5	5	4	2	4	5	6	8	6	55[L]
5101-5500	12	9	8	7	8	5	7	14	7	8	23
5501-6000	14	11	7	6	9	7	11	3	13	13	20
6001-7000	18	25	12	20	12	13	7	10	13	27	25
7001-8000	96	78	15	5	9	4	8	10	9	15	19
8000-10000	NA	NA	55	14	12	5	8	9	17	15	24
10001+	NA	NA	NA	43	33	15	8	20	23	34	29
Total	2654	2873	3052	3269	3490	3773	4032	4332	4583	4798	5008
	Proportions of Beneficiaries by Earnings Interval [b/]										
Zero	.694	.739	.762	.769	.781	.809	.814	.811	.767	.804	.829
Below Exempt Amount	.137	.131	.118	.147	.150	.124	.124	.132	.145	.155	.132
Near Exempt Amount	.057	.052	.051	.031	.026	.032	.032	.023	.014	.013	.011
Above Exempt Amount	.112	.078	.069	.053	.043	.034	.030	.033	.028	.029	.028

[a/] Source: Based on tabulations of OASDHI covered earnings data present in the 1978 CPS-SER-MBR exact match file. Tabulations conducted at The Urban Institute.

[b/] Intervals for those with positive earnings are respectively below, at and above the exempt amount interval as shown in the top part of the table (with the superscript L).

NA Not applicable as maximum taxable earnings fell below this interval.

TABLE 1. SIGNIFICANT ASPECTS OF THE RETIREMENT TEST, 1955 to 1988

	ANNUAL EXEMPT AMOUNT		AGE OF EXEMPTION FROM TEST	AVERAGE HOURLY EARNINGS	ANNUAL EXEMPT AMOUNT ANNUAL WORK HOURS AT AVERAGE EARNINGS	
	UNDER AGE 65	AGE 65			UNDER AGE 65	AGE 65
1955	NA	1200	72	1.71	NA	702
1959	1200	1200	72	2.02	594	594
1964	1200	1200	72	2.36	508	508
1969	1680	1680	72	3.04	553	553
1974	2400	2400	72	4.24	566	566
1979	3480	4500	72	6.16	565	731
1984	5160	6960	70	8.32	620	837
1987	6000	8160	70	8.98	668	909
1988	6120	8400	70	9.32	657	901

Source: Data on retirement test provisions taken from Social Security Administration, Social Security Bulletin: Annual Statistical Supplement, 1987, Table B. Data on average hourly earnings, annual averages for the private nonfarm economy, are from U.S. Executive Office of the President, Economic Report of the President, 1988, Table B-45. Annual work hours estimated as the ratio of the annual exempt amount to average hourly earnings.

NA - Not Applicable. There were no old age beneficiaries younger than age 65 prior to 1957.

Table 2. WORK EXPERIENCES OF MEN AGED 65-69, 1955 TO 1987
(PROPORTIONS OF THE POPULATION)

	WORKERS							DID NOT WORK
	ALL WHO WORKED	F TIME 50-52 WEEKS	F TIME 27-49 WEEKS	F TIME 1-26 WEEKS	P TIME 50-52 WEEKS	P TIME 27-49 WEEKS	P TIME 1-26 WEEKS	
1955	0.682	0.388	0.102	0.074	0.047	0.024	0.046	0.318
1959	0.608	0.290	0.081	0.081	0.052	0.035	0.069	0.392
1964	0.573	0.274	0.064	0.066	0.060	0.036	0.074	0.427
1969	0.577	0.250	0.067	0.063	0.078	0.044	0.074	0.423
1974	0.446	0.186	0.043	0.051	0.076	0.037	0.054	0.554
1979	0.384	0.143	0.031	0.045	0.069	0.033	0.063	0.616
1984	0.353	0.136	0.023	0.044	0.062	0.036	0.053	0.647
1987	0.342	0.127	0.026	0.041	0.060	0.031	0.057	0.658
CHANGE 1955-87	-0.340	-0.261	-0.077	-0.033	0.013	0.008	0.011	0.340

SOURCE: U.S. Bureau of Labor Statistics, Work Experience of the Population, various issues.

TABLE 4. EARNINGS AND POVERTY RATES FOR PERSONS AGED 65-71 IN 1977

LEVEL OF EARNINGS IN 1977	BENEFI-CIARIES	NONBENEFICIARIES				
		TOTAL	DID NOT RETIRE 1978-80	RETIRED 1978-80 AND AGED 66-71 IN 1977: TOTAL	MEN	WOMEN
	WORKER COUNTS					
ZERO	3156	399	368	31	11	20
1-1500	239	14	11	3	2	1
1501-2600	176	9	6	3	1	2
2601-3300	171	3	1	2	1	1
3301-6000	72	15	9	6	3	3
6001 AND ABOVE	45	198	100	98	69	29
TOTAL	3859	638	495	143	87	56
	POVERTY RATES - PERCENT					
ZERO	12.9	24.6	25.0	19.4	*	25.0
1-1500	11.3	*	*	*	*	*
1501-2600	2.8	*	*	*	*	*
2601-3300	5.8	*	*	*	*	*
3301-6000	6.9	*	*	*	*	*
6001 AND ABOVE	2.2	1.5	2.0	1.0	0.0	3.4
TOTAL	11.8	16.5	19.6	5.6	2.3	10.7

SOURCE: Based on tabulations of the 1978 Current Population Survey - Summary Earnings Record - Master Beneficiary Record exact match file done at The Urban Institute.

* Poverty rate not shown because the cell has fewer than 20 persons.

Chairman JACOBS. Mr. Daub.

Mr. DAUB. I wouldn't begin to indicate my feelings are statistically based, but are more a dynamic perception that the work force has dramatically changed. I do not believe as a percent of the total work force there were as many jobs available in 1980 as there were in 1970. So trying to look through that window to what 1990, 1994 looks like when we know what that population curve that you have all studied so well at the Urban Institute—and I have read many of the documents that come from there—the idea that with fewer births and deaths, we see our elderly numbers go from 32 million to 50-plus million people over a 15-year period of time that bothers me not in terms of the safety, solvency and soundness of the trust fund, there are four trust funds that divide the FICA, but it bothers me in terms of the social environment that we ought to be in.

I am not sure I am right, but my perception is that in fact we ought to meet the challenge—you know, robots, computers, lasers and a whole different kind of environment. I could be wrong. We can disagree statistically.

My basic feelings look at a more dynamic environment of where we will be as we continue to deregulate and live longer and older people become more valuable in the work place in some way, if not the sheer fact of the numbers, by their experience and their competency and their stability and regularity and all the things that will help us to have a productivity curve that grows.

You have declining numbers of people at age 18 entering the work force. I am maybe not in disagreement as much as you might think. I try to be more dynamic about looking ahead, and some of my assumptions can be wrong. It is just the idea of what you just said makes more sense. I would like to see it repealed, I think, as a matter of policy.

But I am very willing to appreciate marginwise public policy may not go that far, but as long as we move in that direction to be more progressive about our attitude toward work, and maybe $15,000 or $18,000 is where the next limitation should be. That will be up to this committee to decide long after I have gone. I didn't get to hear your testimony. Forgive me for being tardy on that.

I read your testimony last night, Mr. Entin. Would you care to comment on the relationship of the initial cost of repealing the retirement test and our efforts to balance the budget? I believe the Institute has said using the budget as an excuse for inaction is tantamount to cutting off the nose to spite the face.

Mr. ENTIN. Yes, sir. We did suggest a number of offsets to the costs, and I think a number of the provisions, the minor adjustments to the benefit formulas and computation rules that Commissioner Hardy may have gone into in some detail, would offset a third of the expense right off. The reflow that you will get out of the Joint Tax Committee, is grossly understated because of the static revenue estimates they do without taking account of the GNP changes that would result Those estimates, including GNP changes, if they really were forthcoming, I think would cover another quarter perhaps, or more, of the expense of repeal.

So I don't think it would be that expensive. A phase in would work very nicely, in that every year real economic growth gives the Government an additional $30 billion in revenue, that is, $30 bil-

lion, this year, $60 billion at an annual rate next year, and $150 billion annually by 1993. If you phased the thing in in stages, of course, you would end up only getting to the full $5 billion cost when Government receipts were $150 billion higher That would take 3 percent of the incremental receipts of the Government even if you had no other changes in the benefit computation formula.

I would like to say one thing about the historical record on labor supply. During the period where the earnings test was liberalized, of course, you shifted the marginal effect of it, the point at which it moved away from certain individuals but caught up with certain others. You would expect it to have more effect on work effort for one group and less for another.

Furthermore, during the decades of the mid-1960's to the 1970's or a bit beyond, you had other taxes changing. You had the typical worker moving from combined State and Federal tax rates at the margin of about 25 percent in 1965 up to about 45 percent by 1981, and you had the after-tax wage going down from 75 cents on the dollar to about 55 cents on the dollar.

When you start adding in a 50-percent hit on the earnings limitation, you had the combined after-tax, after-earnings limitation effect leaving the worker 25 cents on the dollar in the 1960's but only about 5 cents on the dollar in the late 1970's. That is a powerful incentive not to work. In the 1980's it was the tax rate reductions and earnings limit restructuring that knocked the penalty down. Thank heaven for small favors.

One other thing on the cost. Again, it is temporary. Under current law, you are raising the delayed retirement credit to where it will be actuarially fair for people age 65 and over. At that point, they can ignore the earnings test, work the extra 2 or 3 years, defer their benefits temporarily and pick them all up when they stop working. At that point, since you are going to be paying them their full lifetime benefits anyway, it doesn't cost you anything to repeal the test.

Mr. DAUB. We increase the penalty for quitting early from 20 percent to 30 percent.

Mr. ENTIN. You also do that for people below the retirement age.

Mr. DAUB. You have to remember in 1983, we also did that. One of the problems was with inflation. It was better to quit at 62 because the time value of money plus inflation made it more valuable to bet on taking 3 years of Social Security, particularly if you were low and middle income, than living those 3 years and taking retirement at age 65. You might be better off quitting early. That was a powerful work disincentive.

We changed that. We penalize you more for quitting early plus we added the inducement of the 8 percent delayed retirement credit, plus, of course, we raised the retirement age starting in the year 2000. We phased that retirement age up to 67. You put all those things together, and I think those were admissions the work force was going to change. One more thing we could do to enhance what we did in 1983 would be to do something about the current limitation on earnings.

Mr. ENTIN. I thank you for reminding me of that. My argument doesn't apply to just age 65 and above. It applies down to age 62.

Mr. DAUB. There is a category of people that quit early, and we changed the penalty from your first table. If you quit early now you receive some percentage down to 80 percent of the full retirement benefits payable at age 65. We have dropped that to a 30-percent penalty if you quit early. That is something people are forgetting.

Mr. ENTIN. It is important that you remind people of that. This was a good change. As it was fully phased in over the next 17 years, you will find each year you look at the earnings test repeal, the estimated cost of it must drop, because once you have fully phased in this delayed retirement credit reform, it doesn't cost anyone to work an extra year, they will pick up their full benefits via the delayed retirement benefit in the years after they stop working altogether, in which case it costs you nothing at that point to repeal the test outright.

So as I say, the cost of repealing the test would be a real cost only for the next 17 years, and it would be declining during that whole period. Basically, it is the current group of retirees which does not now have advantage of this increase in the delayed retirement credit that is suffering. As it comes along, they will suffer less. Why not put them out of their misery now?

Mr. DAUB. One last observation, the answer may be with modest phase ups selecting a date in the future, like 1999 or 2005, for the elimination over a much longer period of time.

Chairman JACOBS. Mr. Entin, you say you were part of this administration?

Mr. ENTIN. I was the Deputy Assistant Secretary for Economic Policy at Treasury.

Chairman JACOBS. Why do you suppose President Reagan disagreed with Commissioner Hardy and in his budget did not submit a request for repeal of the retirement test? Have you any idea?

Mr. ENTIN. I would have to go back and see when the Social Security Administration completed its work on the proposal. I couldn't answer that question. It may not have been ready in time or discussions may not have been finished.

Chairman JACOBS. My understanding is that the discussion was thorough and, after the discussion, the President rejected the proposal and declined to include it in his budget.

Mr. ENTIN. I was not there, I am sorry.

Chairman JACOBS. What would be the tax increase, FICA tax increase to repeal the retirement test say this year effective January 1?

Mr. ENTIN. What would be the tax increase?

Chairman JACOBS. Yes, the FICA tax increase in order to pay for the cost of doing it.

Mr. ENTIN. If you repealed——

Chairman JACOBS. Assuming you wouldn't raid the trust fund for the money that is already there for the purpose already designated under law, I would assume you would agree to a tax increase to pay for the retirement test repeal?

Mr. ENTIN. I doubt very much anyone would propose raising the FICA tax to cover it. I suspect it would be phased in in a way which would have minimal budget impact.

Chairman JACOBS. To cover that minimal impact, whatever the impact might be, if the retirement test were repealed this year, effective January 1, 1989, what would the—what increase in the FICA tax would be required on employees and employers?

Mr. ENTIN. It would have to be be 2.5 percent of 15.3 percent, a couple of tenths of a percent.

Chairman JACOBS. A couple of tenths of a percent. I don't want to hot box you, why don't you send it to us?

Mr. ENTIN. I think that would be about right.

Chairman JACOBS. Would you like to submit that a little bit later?

Mr. ENTIN. I will check the figure. It was a very small number. That is without assuming any feedback applied to the system from the added work effort. That would probably cut the amount in half.

[The following was laid in the record by the staff:]

ESTIMATE OF THE SOCIAL SECURITY ACTUARIES

At the request of the staff of the Subcommittee on Social Security, the Social Security Administration actuaries provided a rough estimate of what tax rate increase would be required if the short-range cost of the proposal offered by the Social Security Administration and the Department of Health and Human Services was financed through an increase in the payroll tax. The proposal would increase the payroll tax rate for employees by 0.125 percent and the tax rate for employers by the same amount. As a result, the current rate of 7.51 percent would be increased to 7.635 percent and the rate for 1990 would be increased from 7.65 percent to 7.775 percent.

This amount was arrived at by dividing the 1-year cost of the provision—$5 billion—by the total payroll of the U.S. workforce—$2 trillion. This provided a combined employer-employee tax rate increase of 0.250 percent.

[The following was received from Mr. Entin:]

Additional Material Submitted by Stephen J. Entin in Response to Questions by Chairman Jacobs at the Social Security Subcommittee Hearing on the Social Security Retirement Test, 9/29/88

Chairman Jacobs asked for a more refined estimate of how much the payroll tax rate would have to be raised to cover the cost of repealing the earnings limitation for beneficiaries aged 65 through 69.

It should be noted first that the OASDI program will be running surpluses throughout the period prior to 2009, by which time the cost of the repeal would become zero due to the increase in the delayed retirement credit scheduled in current law. (This increase will enable beneficiaries to receive, on average, the same lifetime benefits whether they retire at the normal retirement age or later; if the retirement test is still in effect at that time, people may avoid it simply by delaying the date on which they file for benefits, and still receive full lifetime benefits after they cease work.) The OASDI surpluses are far larger than the temporary costs of repeal, and no change in financing would be required to meet the expense.

However, if it is considered desirable to maintain the same unused spending authority in the trust funds after repeal as would have existed without repeal, one could translate the cost of repeal into a percent of taxable payroll and add that amount to the currently scheduled payroll tax rate, for illustration.

In doing so, one would have to make some assumptions: how the proposal would affect tax revenue from the taxation of benefits; how much added work effort and income would occur among the affected beneficiaries, which would affect the flow of payroll tax receipts into the trust funds, and whether added income taxes paid by the affected beneficiaries would be channeled to the trust funds or to the general fund of the Treasury; and whether any cost saving amendments, such as accelerating the increase in the delayed retirement credit, were included in the proposal.

It is reasonable to assume that the offsets suggested in my testimony, as costed out by SSA, and the revenue reflow from added work effort, if channeled to the trust funds, would cover 50 to 60 percent of the cost of repeal. This would result in a net cost of $2 to $2.5 billion in 1990, the year the payroll tax rate is scheduled to rise to 15.3 percent of payroll. Taxable payroll in 1990 is projected to be $2.333 trillion under Alternative II-B assumptions. Thus, the net cost of the proposal could be covered by a temporary increase in the payroll tax rate of 0.1 percent of payroll, to 15.4 percent. This could be scaled back to 15.3 percent gradually over the period through 2009 to reflect the declining cost of the proposal under current law as the delayed retirement credit is increased.

Chairman Jacobs also asked why the Administration did not include repeal of the earnings limitation in its FY 1989 Budget. Upon further reflection, I believe it had something to do with the timing of the SSA proposal, not with respect to the Budget deadline, but with respect to the "Budget Summit Agreement" between the Administration and the Congress. The Agreement did not allow explicitly for the proposal, and the Administration would have been able to proceed only if it could have scored the proposal for budget purposes as a budget neutral provision. Given the static revenue estimation procedures of the Joint Tax Committee, CBO, OMB and Treasury, it would have been ruled out of order to include the substantial tax reflows which the provision would generate through added work effort by beneficiaries. I suspect that this purely arbitrary technical convention is probably what derailed the effort. I discuss the inadvisability of this scoring convention in my submitted statement.

Chairman JACOBS. Exactly. I thought you would want to calculate it thoroughly. Now, on the question of the 65-percent tax rate, if the Defense Department overpays a contractor and requires the contractor to pay some of that back, is that properly classified as taxation or refund of excessive payment?

Mr. ENTIN. That is refund of an excessive payment.

Chairman JACOBS. How is it different here? Under the law, if you work beyond what the law finds allowable and has found allowable for Social Security benefits and you pay back the amount that was overpaid to you, why is that suddenly a tax?

Mr. ENTIN. Overcollecting for work performed is one thing. Having the Government charge you if you attempt to contribute to the GNP——

Chairman JACOBS. The Government recovers overpayment as I understand?

Mr. ENTIN. If you perform extra hours of work past a certain point, the reward to performing that work is markedly reduced. That is a tax on production.

Chairman JACOBS. Sure. When there is an overrun on a Government contract, it is reduced too?

Mr. ENTIN. The expected reward for performing the work was not expected to be that surcharge, just up to what was initially agreed upon.

Chairman JACOBS. I beg your pardon?

Mr. ENTIN. The surcharge was never properly part of the reward in the first place.

Chairman JACOBS. Is excessive payment of the Social Security benefit properly part of the reward for having paid into the system if the condition was the retirement test?

Mr. ENTIN. The value—I am saying it is an unfair condition. The value to the society of the added work——

Chairman JACOBS. A contractor could say it was an unfair condition too?

Mr. ENTIN. The market determines what the value of the item is to the Government. The market also determines what the value is in terms of gross wage of the worker's added service. It is when the Government steps in and imposes taxes that the provider of the service gets less than the social benefit of the labor.

Chairman JACOBS. When you impose a tax on my salary, my salary is something which at least I would argue I earned, right? That is a tax. That is something, money, I got from work I did. The Social Security system's law is not ambiguous, it is quite clear what retirement is, it is just like casualty insurance. You may pay in for 20 years and never have an automobile accident and never get anything back from it, but the terms of the contract were not ambiguous and the mere fact you had been overpaid under the terms of the contract and required to pay back the excess, you are saying that that constitutes the U.S. Government taxation?

Mr. ENTIN. Absolutely. Your salary is supposedly a measure of your contribution to the GNP. As you take home only a fraction of it, you get less than full value, because the Government takes a portion. If another contributor to the GNP faces a much higher tax rate, the tax is not neutrally applied.

Chairman JACOBS. You are accepting your own premise when you say "faces a much higher tax rate." The question is: if you are overpaid by the Government and required to pay back the overpayment, how does that jump into the category of a tax?

Mr. ENTIN. The contractor in the Defense Department and the DOD came to agreement and both signed on the dotted line——

Chairman JACOBS. That is true of the Social Security system too.

Mr. ENTIN. I don't believe someone considering working longer under Social Security is happy with that law and if he had to vote on it and had a one to one deal with you directly, I don't think he would sign onto that agreement.

Chairman JACOBS. The contractor might not be happy with the contract he had to sign, perhaps not too much compensation over there, in some cases may not be happy with that either. The point is it is a contract, at least that is how I hear it argued when I hear the testimony today that we have a right to the benefits, we have the right to the benefits for which we contracted by paying the Social Security tax.

Some people don't pay the Social Security tax.

Mr. ENTIN. If you can find me a piece of paper where the beneficiary signs an agreement to the earnings limitation and was voluntarily in agreement with it, then I would say it is similar to General Dynamics signing with DOD.

Chairman JACOBS. Let's take the case of military service and the draft. If you are drafted to serve in the Army and you are paid $65 a month, is that a contract?

Mr. ENTIN. It is involuntary by its very nature.

Chairman JACOBS. Is that a contract?

Mr. ENTIN. No, I don't think the term can be used in an involuntary transaction.

Chairman JACOBS. If the soldier is paid $60 a month, having been drafted, and they make a mistake, the paymaster makes a mistake and pays him $65 instead of $60 and they dock him from the next month's wages, I don't suppose he has been taxed, he just hasn't paid back the amount the Government overpaid him. Is that a tax?

Mr. ENTIN. No.

Chairman JACOBS. What is the if? That is involuntary. You say Social Security is involuntary. There is an overpayment to the soldier, there is an overpayment under the terms of the law to the Social Security beneficiary. What is the difference?

Mr. ENTIN. The soldier is in no condition to vary his employment.

Chairman JACOBS. But what is the difference in the relationship to the taxpayers of the country who are putting up the money to pay these benefits?

Mr. ENTIN. There is no question they save money, but it is not something either party you have named would be happy with.

Chairman JACOBS. But you see a distinction between the soldier situation and the Social Security beneficiary situation?

Mr. ENTIN. Yes.

Chairman JACOBS. In the one case, there is an overpayment to the soldier involuntarily brought into contract with the Government; in the other case, there is an overpayment to the Social Security beneficiary whom you say was brought in involuntarily into

the contract, but still there is somehow a difference which makes taxation, the recovery of excess payments of Social Security, and not taxation in the case of an overpayment to the drafted soldier. Is that your testimony?

Mr. ENTIN. Yes, sir. I think the variability of hours is quite clear.

Chairman JACOBS. Thank you.

Any further questions?

Mr. DAUB. Just the idea in this last discussion that you both had different definitions, so you were kind of passing each other.

Chairman JACOBS. No, I think the question is whether it is properly defined as tax.

Mr. DAUB. I am trying to sort this out so I am sure I understand you both. You believe that the person who has worked all their life is saying at that point, when they retire, hey, I didn't realize that there would be this big a bite taken out of my future expectation?

Mr. ENTIN. I am simply saying when it gets to that point, it is not worth working. You have practically told them, if you work, you are going to get nothing out of it.

Mr. DAUB. I think the chairman is exploring the point here, and don't take the argument wrong, but the problems of 1978, 1980, and 1981 where outflow from the trust funds were more rapid than the inflow. We determined what the FICA tax was going to be on a lower wage rate, and Congress was not willing to adjust the tax as the cost of living went up, and so there was also pressure on the COLA, and out went the money faster than people were paying in. We just did not adjust to make sure it was right.

Now the expectation of that worker today, when they retire 20 years from now, is a big problem. I don't know whether it is a contract or not, but I know the age of 70 or the age is 65, those artificial boundaries were laws. Were those contracts with people? We told them by the time you are 65, you should have known all your life we were going to force you to retire. We decided we would change that law.

I would hope we could change this one for a good public policy reason.

Mr. ENTIN. There is an interesting table at the back of the testimony showing, and I will use the word under protest, the "contract", the implication of the alternative II-B assumptions in the latest trustee's report, as to what we are promising the beneficiaries. If you do a survey, I am not sure people are going to fully believe those numbers will hold.

Chairman JACOBS. I think when you pay back an overpayment, you are not paying tax, you are just obeying the law.

Our next panel, please come forward.

Mr. DAUB. Thank you very much, gentlemen.

STATEMENT OF MILDRED McCAULEY, MEMBER, BOARD OF DIRECTORS, AMERICAN ASSOCIATION OF RETIRED PERSONS

Ms. MCCAULEY. I am Mildred McCauley, a member of the board of directors of the American Association of Retired Persons. AARP appreciates the opportunity to present its views regarding reform of the Social Security retirement earnings test.

Given the increased longevity and generally improved health of many retirees and the prospect of an aging society, it is important that we find ways to allow older persons to continue making economic contributions. We support changing the retirement test for several reasons.

First, it is particularly burdensome on lower and moderate income persons who rely heavily on Social Security as their primary retirement income source. Many of them work out of necessity and deliberately restrict their earnings to avoid losing benefits. Changing current law would provide these people with a greater measure of economic security.

Not only does the retirement test restrict earnings for some, it also creates problems for working beneficiaries and increases administrative costs for the Social Security Administration. Many people are confused by agency provided explanations of the retirement test and unnecessarily endure financial hardships when an overpayment is recouped.

In addition, the earnings limit is discriminatory. It creates an artificial distinction between the earnings of those below the age threshold and those above it. Some oppose removing the limit because it could be costly to the trust fund in the short term. While total elimination for all beneficiaries would be expensive in the short term, the removal can be phased in to help reduce the initial cost.

Moreover, the cost argument overlooks the potential for added income tax and payroll tax revenue. While a projection of the revenue gains may be difficult because of uncertainties regarding the number of beneficiaries returning to work and the amount of increased earnings, it is clear some additional Federal revenues will be collected.

Others contend changing current law would largely help high-income beneficiaries. However, they may be overlooking a group of moderate income persons who deliberately hold earnings below the threshold. Since these people do not have their benefits reduced, they are not counted as potential beneficiaries of change.

In addition, some question the changing of the program from a wage replacement benefit payable at retirement to an annuity payable at a specified age. However, this view does not take into account the larger national and individual economic needs of an aging society and a changing definition of retirement. Retirement no longer means no work. Now it means exploring options for continued contributions.

All too soon our country will be faced with a serious labor shortage. New jobs requiring technical skills will be unfilled because there are too few skilled workers. Our country needs to respond by doing everything possible to encourage older workers to remain active in the work force.

Given the concerns about the impact on the trust funds of complete elimination, AARP would recommend a phased-in approach that gradually lifts the ceiling amount to a more reasonable limit, approximately double the current limit. Most people who could increase their work effort would benefit by this approach. And the short-term loss to the trust fund would be minimized. Once this new limit is in place, we will be in a better position to evaluate the

further costs and benefits of proceeding toward complete elimination. We urge Congress to move ahead on this issue.

Thank you.

Chairman JACOBS. Thank you.

[The statement of AARP follows:]

STATEMENT OF THE AMERICAN ASSOCIATION OF RETIRED PERSONS

The American Association of Retired Persons (AARP) appreciates the opportunity to present its views regarding the Social Security retirement test. The Association has long supported a change in the Social Security earnings limit issue. Given the increased longevity and generally improved health of many retirees and the prospect of an aging society, it is important that we find ways to open up opportunities for continuing economic contributions from one of our most valuable economic resources: older Americans.

The Earnings limit in Practice

The retirement test limits the amount of earnings from employment that a Social Security beneficiary can receive without penalty. The test applies not only to retired workers, but also to spouses and children of retired workers; and survivors with benefits. In 1988, beneficiaries between 62 and 65 may earn $6,120 without a reduction in benefits; those between 65 and 69 may earn $8,400.

Currently, benefits for a retired worker under age 70 are payable for all months in a year if annual earnings from all types of employment (whether or not covered by Social Security) are equal to or less than the applicable "exempt amount." A special monthly test is applicable in the "initial year of claim" if it produces a more favorable result than the annual test.

Modifications in the Earnings limit

Although Congress has always provided a retirement test in the Social Security program, it has made changes almost from the inception of the program. Originally the law prohibited a person from drawing a benefit for any month in which wages from "regular employment" were received. The term "regular employment", however, was not defined. Moreover, the "regular employment" test was never applied because the law was amended in 1939, before the first monthly Social Security benefits were paid in January 1940. Under the 1939 amendments, a test was instituted under which a month's benefit was withheld for any period in which a beneficiary's earnings exceeded a fixed threshold.

Since that time, the earnings limit has undergone a variety of modifications that have narrowed the category of affected persons. For example, the age at which the earnings limit was eliminated was reduced from 75 years of age to 72 and is now 70. In addition, it was transformed from a simple monthly test to one that measured both monthly and yearly earnings. Also, the penalty for excess earnings above a threshold was altered from a total loss of monthly benefits to a reduction in the benefits. Under current law, beginning in 1990 beneficiaries will have benefits reduced $1 for every $3 of excess earnings, instead of the current $1 reduction in benefits for every $2 earned. Finally, the law now provides for an automatic, annual updating of the retirement test threshold in accordance with changes in annual wages.

Thus, there is ample precedent for reevaluating the retirement test to better meet the needs of older Americans, of society, and our economy.

Increased Work Effort Effects

Most older persons are not in the labor force and may not be affected by a change in the earnings limit. About seven out of eight persons 65 and older do not report any income from earnings. Of those 65 and older with earned income, about 68 percent worked part-time, with only one-third of men 65 years and older with earnings working full-time. Removing the earnings

limit may cause some part-time workers to increase work hours, and also draw some non-workers back into the work force. For others, however, non-participation in the labor force reflects non-economic factors such as poor health or the preference to be fully retired. Thus, most retired Americans are unlikely to re-enter the labor force.

Income effects of removing the earnings limit on older persons

In general, most low and moderate income older persons rely heavily upon Social Security benefits as their primary retirement income source. They tend to have been lower wage earners and therefore were unable to accumulate adequate savings or earn adequate pensions during their working years. As a result, these older persons have little or no non-Social Security income to draw upon during retirement. For those who are capable and have the desire to work above the earnings limit, the opportunity to improve their economic position through employment is constrained by the earnings limit. In the words of one of our affected members who has written us:

> "I am not alone in believing the law restricting the amount earned by Social Security is the most unfair and discriminatory law in our beloved United States. The maximum allowable amount is total earnings, and not take home pay...
> "I am an executive secretary, a widow of one year, and I could not possibly live on the allowable earning and my meager Social Security benefit. Would the government prefer us to live in subsidized low-cost housing, receive food stamps and/or welfare? I am too proud to do that..."

This illustrates only one of several situations in which many older Americans find themselves. The attached case studies (Table 1) illustrate how the elimination of the earnings limit would have different effects on Social Security recipients of varying incomes and work patterns. The following cases look at:

-- low-income earners whose earnings are currently under the earnings limit;

-- moderate-income workers who have the ability to greatly increase earnings;

-- middle-income older workers whose Social Security benefits are now reduced or eliminated through the earnings limit;

-- upper-middle income workers who would increase earnings substantially.

Case one depicts low income wage earners who would be encouraged to increase earned income by the elimination of the earnings limit. Of importance to these older workers is that they would realize the full monetary gain from any increased work effort. The Social Security trust funds could recognize a revenue gain from workers in this situation through higher payroll taxes. However, for some low wage earners, any change in the earnings limit will have no effect on income because many are already working as many hours as their schedule permits, often at the minimum wage.

Case two depicts earners who purposely maintain earnings levels below the thresholds. A clustering of beneficiaries earning around the threshold level has been a characteristic pattern over time. This suggests that beneficiaries choose to restrict their earnings to avoid a penalty.

Those in Case two are able to maintain an adequate standard of living because they also have moderate levels of pension and investment income to supplement their benefits and earnings. An increase in earnings results in additional payroll and income taxes paid with some of that income tax revenue-- that portion caused by the increase in taxable Social Security benefits-- going into the Social Security trust funds.

Case three depicts persons who have not received Social Security benefits because of their high levels of earned income. With the removal of the earnings limit they will now be able to receive Social Security benefits, with no additional work effort. For these persons, the earnings limit is not an employment barrier, but a financial penalty. For these persons, the receipt of benefits will result in higher income tax payments caused by the taxation of one-half of Social Security benefits. These additional revenues will be used to partially offset the losses to the Social Security trust funds that result from the new benefits that are paid.

Case four depicts higher income individuals who, unlike those of the previous example, restrict their earnings in order to draw Social Security benefits. These individuals have the desire to participate to a greater extent in the work force, but their motivation is dampened by the earnings limit. Lifting the earnings limit allows them to increase earnings, but will not increase their Social Security benefits. These persons already pay tax on one-half of their Social Security benefits, so nearly all of the increase in Federal income taxes will go into general revenues. Because these persons are already receiving a benefit, there will be a net gain to the Social Security trust funds as a result of additional payroll taxes paid on their increased earnings.

The attached charts (chart 1 and chart 2) suggest that millions of older low-income persons and households fall into the economic range depicted in case 1; relatively few fall into the case IV category. About one-third of persons between 65 and 69 fall into the middle-income group depicted in cases II and III. However, the number of persons within these income ranges who would take advantage of any change in the earnings limit is difficult to estimate.

One reason for this difficulty is that many older workers do not apply for benefits because they know their earnings exceed the limit. However, a study by the Social Security Administration of 1982 beneficiaries indicated that about one million retired-worker beneficiaries had some or all of their benefits offset by the limit. About 8 percent of beneficiaries were affected by the limit. An additional one-half million who received benefits as dependents and survivors were also affected by the limit. A total of $5 billion in Social Security benefits was offset in 1982 as a result of the limit.

These estimates were made in 1982 when individuals aged 70 and 71 were affected by the earnings limit. Therefore, this estimate is somewhat higher than what may be true today. Also, it does not include those who did not apply for benefits because they knew their earnings exceeded the limit.

The Social Security actuaries estimate that 430,000 persons will receive lower benefits as a result of the earnings limit in 1989. Again, this projection does not include those who would have all of their benefits offset by an earnings limit or those who do not earn more than the threshold amount.

AARP will continue its study of the earnings limit and will be pleased to provide more precise estimates of the affected population when they become available.

Other Problems Created by the Earnings limit

1. Administrative

While the test clearly limits the earnings of a group of beneficiaries, it also results in administrative problems for employed beneficiaries and the Social Security Administration (SSA), the agency responsible for the program. Many of these problems would be avoided by changing the earnings limit.

SSA spends over $200 million a year and uses 8 percent of its employees to monitor income levels. SSA estimates that 60 percent of all overpayments and 45 percent of all underpayments result from the earnings limit. Thus, modifying the limit would reduce Social Security's administrative costs.

For beneficiaries, it would mean less frustration and inconvenience. Our members report that agency-provided explanations of the earnings limit are confusing, especially regarding the first year of retirement. Such misunderstandings create financial and emotional hardships when overpayments must be recouped, especially from a beneficiary who relies upon these earnings as an essential income source. An underpayment also creates a financial hardship.

2. Decreased Productivity

As our society continues to age and the pool of tomorrow's workers fails to keep pace with the demand for labor, older workers should be encouraged to remain in the workforce. The Census Bureau estimates that in 1995, there will be five million fewer 18-to-24 year olds than there are today. At the same time, according to the Labor Department, the economy is expected to generate 16 million new jobs, 12 million of which will require some education, technical training and experience beyond high school. In light of this, former Labor Secretary William Brock has warned of the possibility of a major skills shortage in this country before the end of the century. Not only will the economy benefit from retaining more older workers, but studies show that the more active and more productive persons over 65 tend to remain healthier both physically and mentally than their more sedentary counterparts.

Faced with these demographic projections, our nation should do everything possible to remove employment barriers, reduce age discrimination, change employer attitudes, and eliminate government-enforced disincentives to work for older persons. Efficient use of mature and experienced men and women can make a positive impact upon the general economy.

Implicit in the 1983 Social Security Amendments were strengthened incentives for older Americans to remain in the workforce. The Amendments reduced the earnings limit penalty from a reduction in benefits of $1 for $2 of excess earnings to $1 for $3 in 1990; it raised the retirement age to 67 by 2027; and it phased-in an increase in the delayed retirement credit (DRC) from 3 percent to an actuarially fair 8 percent by 2008. However, these are future changes and do little to alleviate the impact of the earnings limit for today's retired worker.

3. Discriminations against certain groups of beneficiaries.

Currently, retirees who continue to work beyond age 70 receive full benefits without regard to their earnings. Why should a slightly younger retiree earning the same amount face a penalty? This creates a needless distinction.

Also, some retirees are in a position to avoid the penalty by taking advantage of unique circumstances. While undocumented, there have been many anecdotal accounts of beneficiaries

arranging to receive some part of their wages in cash and not properly reporting their full earnings to SSA. Similarly, other retirees can defer earnings until age 70 although services were rendered earlier. A few others may use creative ways to transform self-employment earnings into unearned income.

Spouses and dependents of beneficiaries have their benefits reduced when a worker's earnings exceed the threshold. Thus, beneficiaries with families are penalized still further. Also, working spouses' benefits are reduced if their own earnings exceed the threshold.

Looking at the Options

For years the defenders and critics have been debating the merits of the earnings limit. AARP believes that it is time for Congress to seriously examine the recommendations to change the earnings limit.

1. The Cost Argument

Some oppose removing the earnings limit because it could be costly to the trust funds over the short term. While total elimination for all beneficiaries would be expensive, the removal can be phased-in to help reduce the cost.

The Association has advocated changing the limit only for those affected over 65. As the retirement age for full benefits moves up, we would support any subsequent upward revisions needed to reflect the retirement age defined by Social Security. Such a modification would reduce the adverse impact on the trust funds.

The cost argument overlooks the lost income and payroll tax revenue to the federal government. While a projection of the revenue gains may be difficult because of the uncertainties regarding the numbers of beneficiaries returning to work and the amount of their increased earnings, it is clear that additional federal revenues will be collected. The primary source would be the income tax, the payroll tax and, in some cases, revenue from the taxation of Social Security benefits for those individuals whose adjusted gross income exceeds $25,000 income for singles and $32,000 for a couple. This additional revenue and reduced administrative costs help offset the cost of the change.

2. Changed Nature of System

The second major argument advanced in opposition to eliminating the limit is that such a change would, in turn, alter the nature of the system from a wage-replacement social insurance benefit payable at retirement to an annuity payable at a specified age. Those who make this argument view Social Security dollars as intended only for the replacement of lost wages due to disability, retirement or death and look upon the earnings limit as the essential mechanism to maintain the retirement element of the program. However, this view does not take into account our larger national and individual economic needs.

3. Benefit Distribution

The third major argument advanced in opposition to elimination of the test is the benefit distribution argument. These critics see most of the additional benefits going to high income individuals.

However, there is a large group of beneficiaries who are of moderate income that the supporters of the earnings limit choose to ignore. The studies that have been done document that a considerable number of those working older Americans who earn at or near the limit deliberately hold their earnings down and drop

out of the labor force rather than bear the high tax rate that the test and taxes impose on earnings over the threshold. Since these people do not actually have their Social Security benefits reduced, they are not counted as potential beneficiaries of eliminating the limit. While the distribution of additional Social Security dollars would help those with high wages, changing the earnings limit also provides additional income for those moderate income persons who choose to hold down their earnings and those beneficiaries whose low monthly benefits require them to work.

4. Fixed Number of Jobs

Finally, although rarely argued in an explicit manner, the earnings limit is defended as a means of improving the employment prospects of younger workers. This reasoning reveals a belief that the earnings limit opens up positions for younger workers and keeps the retired from re-entering the labor market to compete for jobs, and perhaps offering their experience and skilled labor at below market rates. In our opinion, this theory is incorrect. The economy has been able to accommodate an increased number of workers in the past, and it should be able to do so in the future when our population will contain proportionately more older persons.

Conclusion

AARP supports an immediate and substantial raise in the earnings limit for persons over age 65. It would improve the lives of many retirees not only economically but also physically and psychologically. Moreover, modification represents good policy for an increasingly older society.

Given the concerns about the impact on the trust funds of complete elimination, we would recommend a phased-in approach that gradually lifts the ceiling amount to a more reasonable level, approximately double the current limits. Most people who would increase their work effort would benefit by this approach, and the short-term loss to the OASI trust funds would be minimized. Once this new limit is in place, we will be in a much sounder position to evaluate the further costs and benefits of proceeding toward complete elimination. We urge Congress and the Administration to move ahead on this issue.

Case Studies of Lifting Earnings Test in 1988
for an individual 67 years of age
living in the State of Minnesota

	Case 1		Case 2		Case 3		Case 4	
Taxable income by source	earned	$8,400	earned	$8,400	earned	$25,000	earned	$ 8,400
	unearned	0	unearned	9,000	unearned	6,000	unearned	25,000
	SS benefits	3,600	SS benefits	3,600	SS benefits	0	SS benefits	10,000
Expected change from removing earnings test	earned	$12,000	earned	$15,000	earned	$25,000	earned	$25,000
	unearned	0	unearned	9,000	unearned	6,000	unearned	25,000
	SS benefits	3,600	SS benefits	3,600	SS benefits	9,000	SS benefits	10,000
Change in benefits		$0		$0		$9,000		$0
Net effects	income	$3,600	income	$6,600	income	$9,000	income	$16,600
	SS taxes	540	SS taxes	991	SS taxes	0	SS taxes	2,493
	Fed taxes	540	Fed taxes	1,154	Fed taxes	1,260	Fed taxes	5,033
	State taxes	216	State taxes	496	State taxes	0	State taxes	1328
Overall gain or (loss) to individual		$2,304		$3,959		$7,740		$7,746
Overall gain or (loss) to SS trust funds		$540		$1,103		($7,740)		$2,670

* The State of Minnesota does not tax Social Security benefits.

Case 1 -- This individual was intentionally working up to the earnings limit. Although he was willing to work more, the earnings limit caused him to lose at least one-half of what he could have earned.

Case 2 -- This individual can change his work behavior because he had been working part-time and could increase the number of hours in employment.

Case 3 -- This individual was not drawing Social Security benefits because his earnings were so far above the earnings limit that it was not worthwhile to draw benefits.

Case 4 -- This individual can easily adjust to increase earnings.

For further information see attachments concerning explanation of case studies table, income distribution of those 65 years and older, and detailed information on the elimination of earnings test and other proposals.

Chart 1

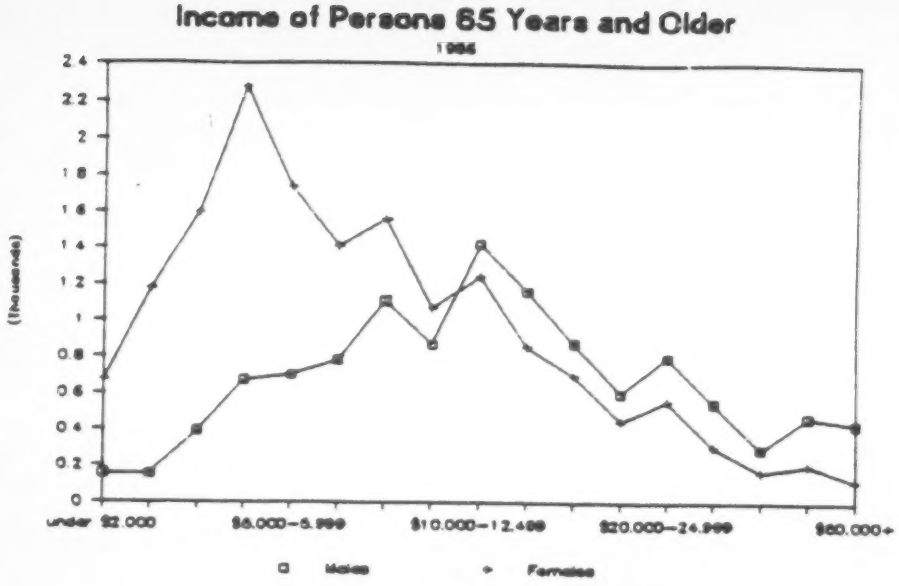
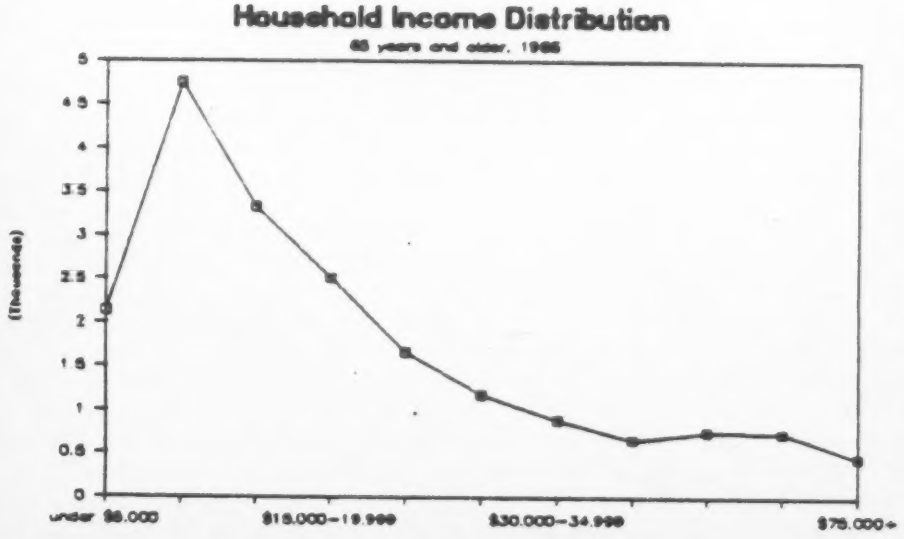


Chart 2



Source: U.S. Bureau of the Census, Current Population Reports, Series P-60, No. 157, Money Income and Poverty Status of Families and Persons in the United States: 1986 (Advance Data from the March 1987 Current Population Survey), U.S. Government Printing Office, Washington, DC 1987.

Chairman JACOBS. Ms. McKenna.

STATEMENT OF THERESA McKENNA, DIRECTOR OF INFORMATION SERVICES, NATIONAL COUNCIL OF SENIOR CITIZENS

Ms. MCKENNA. My name is Theresa McKenna. The National Council of Senior Citizens appreciates this opportunity to address the issue of the Social Security retirement test. We commend Chairman Jacobs for asking the Congressional Budget Office [CBO] to analyze this issue and for holding today's hearing. After careful consideration, the National Council of Senior Citizens has concluded that modification of the Social Security retirement test is not warranted at this time.

Social Security retirement benefits were designed to protect workers against the loss of income in old age due to retirement. For this reason, the retirement test was designed to determine whether or not a worker was substantially retired and, thus, entitled to benefits. To have made Social Security an annuity program permitting the payment of benefits to people with unlimited earnings after retirement would have required much higher contributions from workers, employers and the self-employed than they have been paying all these years.

According to the CBO analysis, "fewer than one in 10 people aged 65 through 69 who are eligible for Social Security benefits is affected by the earnings test, and the characteristics of those affected are quite different from those of the average beneficiary." They determined that, "While only about one-eighth of all beneficiaries had family incomes in 1986 above $42,000, more than 40 percent of those affected by the earnings test had incomes above that level. In contrast, nearly 40 percent of all beneficiaries had incomes below $15,000 compared with only 5 percent of people with earnings above the exempt limit."

The CBO points out that, even under the smallest increase in the earnings limit, only a small fraction of those made exempt would have low incomes. Less than half would be in families with incomes below $25,000—a level which is still considerably higher than median income of all elderly households. Only a quarter of all elderly households have income exceeding $25,000 annually.

The most common reason given for repeal of the earnings test is that it is a disincentive to the continued employment of older workers. Proponents argue that the test represents a prohibitive tax on earnings at the margin, causing workers to deliberately hold down their work level to avoid loss of benefits or seek to be paid "under the table," allowing them to avoid reporting their full earnings. But a study by the Congressional Research Service, released earlier this year, concluded that there is simply little or no data about these behavioral assumptions.

Furthermore, for low-wage earners, the earnings test is no disincentive because they are unable to earn up to the allowable level. A person working full time, year round, at the minimum wage of $3.35 an hour, would earn just $6,700—well below the earnings threshold.

Elimination of the earnings test will not bring jobs to depressed areas or retrain displaced workers for new jobs. It will not end a

still-pervasive bias by many employers against hiring and promoting older workers. And, unfortunately, too many older workers continue to find themselves coerced into early retirement.

Better enforcement of age discrimination laws, more adequate job training or retraining for older workers and more funding for the senior community service employment program, title V of the Older Americans Act, would do much more to encourage the continued employment of older workers.

According to the CBO's analysis, elimination of the retirement test for persons 65 to 69 would cost nearly $24 billion between 1989 and 1993. Even raising the limit to $10,000 in 1989 would cost about $300 million annually.

Our nation's attempt to control the Federal budget deficit has forced all new spending proposals to be closely scrutinized. The cost of modifying the earning test, therefore, would compete with providing job opportunities or a better standard of living for low-income senior citizens.

In an era of budget constraints, spending $24 billion to give higher Social Security benefits to a very small number of persons with higher than average incomes is not justifiable. It is unlikely that repeal would bring new workers into the labor force, although it might increase the work effort of a small group of workers. Even so, in 1990, the test will be significantly liberalized, allowing greater earnings retention by older workers. Further modification of the test now would be, in our view, costly and ill advised. We urge Members of Congress who seek to promote greater work effort by older persons to seek other alternatives.

[The statement of Theresa McKenna follows:]

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Social Security Retirement Test

Statement by

Theresa McKenna
Director of Information Services

Before the

Social Security Subcommittee
Ways and Means Committee

September 29, 1988

Washington, D.C.

First Vice President, Dr. Mary C. Mulvey, Providence, Rhode Island Second Vice President, George J. Kourpias, Washington, DC
Third Vice President, Dorothy Walker, Detroit, Michigan Fourth Vice President, Everett W. Lehmann, Washington, DC
Secretary-Treasurer, Jack Turner, Detroit, Michigan General Counsel, Robert J. Mozer, New York

The National Council of Senior Citizens appreciates this opportunity to address the issue of the Social Security retirement test. There has been considerable interest recently as to whether the retirement test should be eliminated. In evaluating this issue, we believe it is important to consider why the test exists and how it works, who it affects, the distributional impact and cost of its repeal and an assessment of other options that may exist. We commend Chairman Jacobs for asking the Congressional Budget Office (CBO) to analyze this issue and for holding today's hearing. After careful consideration, the National Council of Senior Citizens has concluded that modification of the Social Security retirement test is not warranted at this time.

Why is There a Retirement Test and How Does it Work?

Social Security retirement benefits were designed to protect workers against the loss of income in old age due to retirement. For this reason, the retirement test was designed to determine whether or not a worker was substantially retired and thus entitled to benefits. To have made Social Security an annuity program permitting the payment of benefits to people with unlimited earnings after retirement would have required much higher contributions from workers, employers and the self-employed than they have been paying all these years.

The original concept of the retirement test has been modified many times, gradually allowing retirees to earn greater amounts of income without losing their Social Security benefit.

Under present law, an older worker can earn up to a specified income level with no loss of Social Security benefits. In 1988, this level is $6,120 for workers 62 to 64; $8,400 for workers 65-69. Earnings in excess of these amounts reduce the beneficiaries' Social Security payment by $1 for every $2 of earned income. This means a worker age 65-69, with an average Social Security payment of $500 a month, would not lose all benefits until he or she earned $20,400. The earnings levels are indexed automatically every year. Once a worker attains the age of 70, he or she may earn unlimited income with no loss of Social Security benefits.

Who is Affected by the Earnings Test?

According to the CBO analysis, "fewer than one in ten people aged 65 through 69 who are eligible for Social Security benefits is affected by the earnings test, and the characteristics of those affected are quite different from those of the average beneficiary." They determined that, "while only about one-eighth of all beneficiaries had family incomes in 1986 above $42,000, more than 40 percent of those affected by the earnings test had incomes above that level. In contrast, nearly 40 percent of all beneficiaries had incomes below $15,000, compared with only five percent of people with earnings above the exempt limit."

The study looked at the approximately 600,000 persons aged 65 to 69 who received lower benefits because of the earnings test. The CBO profile found these persons more likely to be male, to live with their spouses, to have family incomes above $32,000, and to have family incomes above four times the poverty threshold (about $21,000 for a single person and about $26,500 for a couple). Significantly, while roughly one-third of comparable Social Security recipients had incomes below 200 percent of the poverty line (about $10,500 for single persons; $13,300 for couples), only one percent of those affected by the earnings test had incomes at such levels.

The CBO numbers are comparable to those reported last year by the House Republican Research Committee, based on data from the Social Security Administration. They determined that beneficiary families for whom repeal of the earnings test would have no impact had median income of $14,700; those who would receive additional benefits had median incomes of $27,700; and those who currently lose their entire benefit (and would, therefore, gain the most from repeal of the test) had median income of $37,700.

According to the "Social Security Bulletin," workers with higher earnings before entitlement to Social Security benefits have higher earnings after entitlement and are also more likely to continue to work. Consequently, NCSC has long been concerned that repeal of the earnings test would provide a windfall benefit to a small percentage of older persons with, presumably, the least need for additional income and the greatest ability to increase their income through work. This concern is sustained by the CBO analysis. The report, in examining the impact of modifying and eliminating the earnings test, found that, while small increases in the earnings limit primarily benefit lower-income families, larger increases or repeal primarily benefit higher-income families.

For example, the CBO reports that about half of affected people in families with annual incomes below $15,000 would not have had their benefits reduced if the earnings limit had been $9,000 in 1986. That level would have exempted just five percent of affected people with family incomes above $42,000. Measuring the income of affected households relative to the poverty threshold, CBO found that doubling of the earnings test in 1986 would have exempted virtually all people with family incomes below 300 percent of poverty, while leaving about two-thirds of those with incomes above four times the poverty level subject to benefit reductions.

Even so, the CBO points out that, even under the smallest increase in the earnings limit, only a small fraction of those made exempt would have low incomes. Less than half would be in families with incomes below $25,000--a level which is still considerably higher than median income of all elderly households. Only a quarter of all elderly households have income exceeding $25,000 annually. Raising the earnings limit at the lower end would, however, disproportionately benefit persons who are widowed or were never married, particularly women.

Would Repeal of the Earning Test Encourage Continued Employment of Older Persons?

The most common reason given for repeal of the earnings test is that it is a disincentive to the continued employment of older workers. Proponents argue that the test represents a prohibitive tax on earnings at the margin, causing workers to deliberately hold down their work level to avoid loss of benefits or seek to be paid "under the table," allowing them to avoid reporting their full earnings. But a study by the Congressional Research Service, released earlier this year, concluded that there is simply little or no data about these behavioral assumptions.

Furthermore, for low-wage earners, the earnings test is no disincentive because they are unable to earn up to the allowable level. A person working full time, year-round, at the minimum wage of $3.35 an hour, would earn just $6,700--well below the earnings threshold. Many older workers prefer part-time employment. A person could earn 2-1/2 times the minimum wage, working 20 hours a week, year-round, and still not exceed the threshold.

It is also relevant to note that, while many older persons need and want to continue working, the trend in this country has been toward earlier retirement. According to an analysis in the "Social Security Bulletin," retirement as late as age 65 is becoming somewhat unusual. For many, particularly those with adequate incomes, early retirement is voluntary. For others,

health limitations, market forces, or physically demanding occupations which become more difficult to maintain with advancing age compel retirement.

Elimination of the earnings test will not bring jobs to depressed areas or retrain displaced workers for new jobs. It will not end a still-pervasive bias by many employers against hiring and promoting older workers. And, unfortunately, too many older workers continue to find themselves coerced into early retirement.

Better enforcement of age discrimination laws, more adequate job training or retraining for older workers and more funding for the Senior Community Service Employment Program, Title V of the Older Americans Act, would do much more to encourage the continued employment of older workers.

The Title V program provides part-time community service jobs for low-income older workers. These minimum-wage jobs provide vital opportunities for about 65,000 older persons of limited incomes who, without such assistance, would often not have the skills or opportunities to find employment on their own. Current Federal spending on this necessary and effective program amounts to just $331 million a year and, while the FY 1989 spending level will increase to $344 million, it will only allow for the retention of current workers after accounting for inflation. Many more low-income older persons could benefit from this program, if additional revenues were allocated for its expansion.

All that aside, as a result of 1983 amendments to the Social Security Act, changes to the earnings test are already scheduled to take place. In 1990, workers will have their benefit reduced one dollar for every three dollars of earnings over the exempt level. In addition, liberalization of a work incentive called the "delayed retirement credit" has already been enacted. At present, workers who delay their retirement beyond the "normal" retirement age (currently age 65) receive a three percent annual increase in their Social Security benefit once they retire. Between 1990 and 2009, this credit will gradually increase to eight percent. This is the level that has been actuarially determined to fully compensate workers for lost benefits once they retire.

Fiscal and Political Ramifications of Repeal

According to the CBO's analysis, elimination of the retirement test for persons 65 to 69 would cost nearly $24 billion between 1989 and 1993. Even raising the limit to $10,000 in 1989 would cost about $300 million annually. According to Social Security Administration estimates, including the 62 to 64 age group, which some have proposed, would approximately double these costs.

The 1980s have been the decade of the deficit. Our nation's attempt to control the Federal budget deficit has forced all new spending proposals to be closely scrutinized. The cost of modifying the earnings test, therefore, would compete with providing job opportunities or a better standard of living for low-income senior citizens.

There are political consequences as well. Just last week, National Economic Commission co-chair Robert Strauss made headlines when he suggested that reductions in Social Security would have to be part of a true deficit reduction package. Those of us who are concerned with preserving Social Security benefits for current and future beneficiaries fear a possible political backlash from proposals such as the earnings test modification.

In an era of budget constraints, spending $24 billion to give higher Social Security benefits to a very small number of persons with higher than average incomes is not justifiable. It is unlikely that repeal would bring new workers into the labor force, although it might increase the work effort of a small group of workers. Even so, in 1990, the test will be significantly liberalized, allowing greater earnings retention by older workers. Further modification of the test now would be, in our view, costly and ill-advised. We urge members of Congress who seek to promote greater work effort by older persons to seek other alternatives.

Chairman JACOBS. Thank you, Ms. McKenna. I think, Mr. Pollack and Ms. Costello, we are going to have to break while we vote.

[Recess.]

Chairman JACOBS. OK, Mr. Pollack.

STATEMENT OF RONALD F. POLLACK, EXECUTIVE DIRECTOR, VILLERS ADVOCACY ASSOCIATES, ACCOMPANIED BY CYNTHIA B. COSTELLO, EMPLOYMENT AND VOLUNTARISM COORDINATOR

Mr. POLLACK. Thank you, Mr. Chairman. Thank you for returning. I appreciate you delaying your lunch. I am tempted to alleviate your burden by saying ditto to Ms. McKenna's testimony, but rather than do that, let me give you a few words about our perspective on the issue.

The Villers Advocacy Associates represents in particular the concerns of lower income citizens. From our perspective the present system is a relatively good one. The earnings test makes it possible for those few low- and moderate-income beneficiaries who do remain in the labor force to augment their Social Security benefits with earnings. However, it does not allow upper income older persons to continue earning a high salary and collect Social Security at the same time.

We urge Congress to oppose the recent proposals for repeal or relaxation of the earnings test. There are several reasons for our position. First, most of those who would benefit directly from these modifications have relatively high earnings.

Second, there is little evidence that these modifications would encourage low- and moderate-income older persons to reenter the labor force.

Third, these modifications are too costly. Older persons would be better served by employment programs targeted at those who need employment.

Let's turn to each of those points. Our first reason for opposing modification of the earnings test is that most of those who would benefit directly have relatively high earnings. The recent Congressional Budget Office report stated that at least 72 percent of those who would benefit have incomes greater than three times the poverty level. That is greater than about $15,800 for a single person and just under $20,000 for a couple.

The table that we have provided at the end of our testimony verifies the statistics that Ms. McKenna provided. It shows that nearly 40 percent of the beneficiaries in the Social Security program had incomes below $15,000 in 1986. Yet, these beneficiaries represented only 5 percent of the persons with incomes above the earnings limit.

Looking at the highest income people as a comparison, those with incomes above $42,000, only one-eighth of the beneficiaries had incomes above $42,000 but they represented over 40 percent of the people with earnings above the earnings limit. This means that as we liberalize the earnings test, liberalize it, disproportionately and overwhelmingly these benefits will go to people whose income levels are at the highest levels in the Social Security system and whose behavior is not likely to be modified by this additional windfall. In effect, it is a poor cost benefit that is being provided.

Our second reason for opposing modification of the earnings test is that there is little evidence that low- and moderate-income beneficiaries would reenter the labor market as a result. Most low-income beneficiaries aren't working presently. A variety of factors discourage them from seeking employment. These include health problems, lower education levels, a history of intermittent employment even before so-called retirement, and dependent care responsibilities. There is little reason to assume that the labor market behavior of these low-income beneficiaries would change significantly if the earnings test were modified.

Among moderate-income beneficiaries there is a small group who would benefit from the modification of the earnings test. These are the beneficiaries with earnings just below the limit who deliberately hold down their earnings or hours of work to avoid the penalty. However, this groups accounts for a very small percentage of the total number of beneficiaries.

If the earnings test were modified it is likely that this group of beneficiaries would increase their work effort accordingly. However, there is little reason to assume that new middle-income beneficiaries would reenter the labor market. The increase in the exempt amount between 1977 and 1982 induced few beneficiaries to return to the labor force.

Our third reason for opposing modification of the earnings test is the cost. Most of the proposals for repeal or relaxation of the earnings test would cost billions of dollars. Proponents argue that the cost would be largely offset by the increased income and payroll taxes paid by retirees who entered the labor market. However, the Social Security Administration estimates that new revenues would offset only ten to fifteen percent of the additional outlays required.

If the Social Security trust fund is to remain in balance, an increase in the Social Security tax would be required to pay for modifications in the earnings test.

As a costly initiative, modification of the earnings test also could fuel a backlash against Social Security. It is this point that Dr. Flemming made. I don't think he had as much of an opportunity as both of you wanted to respond. If it came to light that older people earning $50,000 salaries were also collecting Social Security benefits, this could give legitimacy to the Social Security critics. It might lead to increased interest in limiting benefits for the middle class as well as the wealthy.

Social Security advocates, I believe, fear that such an idea would undermine potential support for the Social Security program. This could jeopardize benefits for low- and moderate-income beneficiaries as well.

Rather than spending billions of dollars on modifying the earnings test, Congress should investigate employment programs targeted at those who need employment. One alternative would be to improve job training programs for older workers. Another would be to increase funding for title V of the Community Service Employment Program.

Before taking any of these actions we urge Congress to carefully examine the distributional and fiscal impact of both the current earnings test and any modifications to it.

One last word. We believe, in fact, that Congress should look again at the changes enacted in the 1983 amendments to Social Security and due to go into effect in 1990. There is little evidence that the lowering of the benefit reduction ratio and the increase in the delayed retirement credit will induce beneficiaries to increase their labor force participation. Those who will benefit from those changes are primarily higher income retirees who would have remained in the labor force regardless. These benefits are not justified when weighed against the cost to the Social Security trust fund.

I have no illusion that Congress will leap to make those changes. But I do think from the perspective of the distributional impact and the impact on the goals I think that all of us in this room share—that is, increasing opportunities for seniors to lead productive lives—there is serious reason to question whether the lowering of the benefit reduction ratio and the increase in the delayed retirement credit will achieve the intended results.

In conclusion, we urge Congress to consider reversing or delaying the changes legislated in the 1983 amendments, particularly the lowering of the benefit reduction ratio. It would certainly be unwise and premature to implement further modifications in the Social Security earnings test without first undertaking a serious assessment of the costs and the benefits.

Thank you.

[The statement of Mr. Pollack follows:]

REPEAL OF THE EARNINGS TEST
A BAD IDEA FOR BENEFICIARIES

Testimony by

Ronald P. Pollack
Executive Director
VILLERS ADVOCACY ASSOCIATES

before the

SUBCOMMITTEE ON SOCIAL SECURITY

COMMITTEE ON WAYS AND MEANS

Washington, D.C.
Thursday, September 29, 1988

Mr. Chairman and members of the Subcommittee, thank you for inviting me to testify before you today as part of this important hearing on the social security earnings test.

Villers Advocacy Associates represents low-income senior citizens. From our perspective, the present system is a relatively good one. The earnings test makes it possible for those few low- and moderate-income beneficiaries who do remain in the labor force to augment their social security benefits with earnings. However, it does not allow upper-income older persons to continue earning a high salary and collect social security benefits at the same time.

In recent years, various proposals have been developed calling for the repeal or relaxation of the earnings test. Some of these proposals call for repeal of the earnings test altogether. Others call for gradually raising the earnings limitation.

We urge Congress to oppose the recent proposals for repeal or relaxation of the earnings test. There are several reasons for our position. First, most of those who would benefit directly from these modifications have relatively high earnings. Second, there is little evidence that these modifications would encourage low- and moderate-income older persons to reenter the labor force. Third, these modifications are too costly. Older persons would be better served by employment programs targeted at those who need employment.

Let me consider each of these arguments in turn:

Most of those who would benefit from modification of the earnings test have high earnings:

A recent report from the Congressional Budget Office showed that relatively few social security beneficiaries are affected by the earnings test. Almost one-fifth of potential Social Security recipients aged 65 through 69 had some earnings in 1986. However, less than 10 percent of these received lower benefits because of the earnings test.

Most of those affected by the earnings test in 1986 had higher-than-average family incomes. Only about one-eighth of all beneficiaries had family incomes above $42,000 in 1986. However, more than 40 percent of those affected by the earnings test had

incomes above 42,000. By contrast, nearly 40 percent of all beneficiaries had incomes below $15,000. Of those with incomes below 15,000, only 5 percent had earnings above the exempt limit. (see Figure 1).

Further evidence that the earnings test affects primarily those with higher incomes is found by measuring income relative to poverty thresholds. In 1986, the poverty threshold for a single person age 65 or over was $5,255. For a two-person family headed by a person aged 65 or over, the poverty threshold was 6,630.

In 1986, beneficiaries with family incomes above four times the poverty threshold made up just over one-fourth of all beneficiaries. However, they constituted nearly three-fourths of those affected by the earnings test. Conversely, those with incomes below twice the poverty threshold represented one-third of all beneficiaries. However, these beneficiaries represented barely 1 percent of those with earnings above the exempt level. (see Figure 2).

If the earnings test were repealed or relaxed, most of the gains would go to people with family incomes many times higher than the poverty threshold. At least 72 percent of the people who would benefit have incomes greater than three times the poverty level -- that is, greater than about $15,800 for a single person and about $19,900 for a couple.

<u>There is little evidence that repeal or relaxation of the earnings test would encourage significant numbers of low- and moderate-income older persons to reenter the labor force:</u>

Proponents argue that repeal or relaxation of the earnings test would help older persons by providing an incentive to reenter the labor market. However, common sense and past practice suggests that modification of the earnings test would do little or nothing for low- and moderate-income older persons.

Most low-income beneficiaries aren't presently working. They are unlikely to return to the labor force if the earnings test were repealed or the limit were raised. Low-income beneficiaries between the ages of 65 and 69 could be earning up to $8400 a year now without jeopardizing their social security benefits. A variety of factors discourage them from seeking employment. These include health problems, lower educational levels, a history of intermittent employment, and dependent care responsibilities.

When previous changes were made in the earnings test, low-income beneficiaries did not return to the labor market. Under the Social Security Amendments of 1977, the annual exempt amount was raised to $4,000 in 1978 and by $500 increments in successive years, until it reached $6,000 in 1982. These increases had no impact on those few low-income beneficiaries who were in the labor force because their earnings were already sufficiently low to exempt them from the earnings test. Nor did the increase in the exempt amount induce new low-income beneficiaries to reenter the labor market. There is therefore little reason to think that further modification of the earnings test would cause low-income beneficiaries to reenter the labor market.

There is a small group of beneficiaries with earnings in the middle of the earnings distribution who would benefit from modification of the earnings test. These are the beneficiaries with earnings just below the limit who deliberately hold down their earnings or hours of work to avoid the penalty. They accounted for only 1.1% of beneficiaries in 1980.

When the exempt amount was raised in 1977, some beneficiaries with earnings near the exempt amount did increase their hours of work and earnings. If the earnings test were modified, it is reasonable to assume that middle-income beneficiaries with earnings near the annual exempt amount would increase their work effort correspondingly. However, it is unlikely that significant numbers of new beneficiaries would reenter the labor market.

Rather than spend billions of dollars on modification of the earnings test, Congress should support employment programs targeted at those who need employment:

Most of the recent proposals for repeal or relaxation of the earnings test would cost billions of dollars. Proponents argue that these costs would be largely offset by the increased income and payroll taxes paid by retirees who reenter the labor force. However, the Social Security Administration estimates that new revenues would offset only 10 percent to 15 percent of the additional outlays required. If the Social Security Trust Fund is to remain in balance, an increase in the Social Security tax would be required to pay for modifications in the earnings test.

As a costly initiative, repeal or relaxation of the earnings test also could fuel a backlash against social security. If it came to light that older people earning $50,000 salaries were also collecting social security benefits, this could give legitimacy to social security's critics. It might lead to increased interest in limiting benefits for the middle class and the wealthy. Social security advocates fear that such an idea would undermine potential support for the social security program. This could jeopardize benefits for low- and moderate-income beneficiaries as well.

Rather than spend billions of dollars on modifications in the earnings test, Congress should investigate employment policies and programs targeted at those who need employment. One alternative would be to improve job training programs for older workers. The major job training programs for older workers, administered under the Job Training Partnership Act (JTPA), are inadequate. Only 8 percent of the total JTPA program participants are age 55 and over, even though this group makes up 20 percent of those laid off during the year and 13 percent of the total unemployed. Older workers need a comprehensive job training program focused on the development of new skills for a changing labor market.

A second alternative would be to increase funding for the Title V Community Service Employment Program. This program provides part-time community service jobs for approximately 62,000 low-income older workers. The current federal spending for this important employment program is only $336 million. By doubling the federal commitment to the Title V program, many more low-income people could gain access to paid employment.

Conclusion

Repeal or relaxation of the earnings test would not be in the interest of most older persons. Those who would benefit are primarily individuals with relatively high incomes. Increasing their benefits would be an unjustified allocation of limited resources. Social security beneficiaries would be better served by job training and employment programs targeted at those who need employment.

Before taking any action, Congress should carefully examine the distributional and fiscal impact of both the current earnings test and any modifications in it. In addition, Congress should

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look again at the changes legislated in the 1983 Amendments to Social Security and due to go into effect in 1990. At that time, the benefit reduction ratio on earnings above the earnings limit will be reduced from 50% to 33.3% for beneficiaries between the ages of 65 and 69. And the delayed retirement credit will be gradually raised from 3% to 8%, giving those who delay retirement until age 70 full credit for forgone benefits.

When Congress passed the 1983 Amendments to Social Security, it was assumed that these changes would induce new beneficiaries to reenter the labor market. However, past practice raises serious questions about whether these changes will produce the intended effect. We have no direct evidence regarding the effect of the change in the benefit reduction ratio on beneficiaries' labor market behavior. We do know, however, that when the annual exempt amount was raised significantly in 1977, few beneficiaries reentered the labor market. There is therefore no logical reason to assume that the lowering of the benefit reduction ratio will precipitate a change in the labor market behavior of beneficiaries.

Nor is it likely that the increase in the delayed retirement credit will affect beneficiaries' behavior. A delayed retirement credit is already in effect for younger beneficiaries between the ages of 62 and 64. This credit has not been sufficient to reverse the trend toward early retirement for older persons in this age group. There is therefore little reason to assume that the increase in the delayed retirement credit for beneficiaries between the ages of 65 and 69 will affect their labor market behavior either.

Past experience suggests that modifications in the earnings test provide insufficient incentive to attract significant numbers of beneficiaries back into the labor force. Other factors -- including poor health, inadequate job opportunities, and the positive value attached to retirement itself --push older workers toward retirement. Therefore, those most likely to benefit from the lowering of the benefit reduction ratio and the increase in the delayed retirement credit are higher-income retirees who would have remained in the labor force, with or without the changes. These benefits are not justified when weighed against the cost to the Social Security Trust Fund. Social security actuaries estimate that the change in the benefit reduction ratio alone will cost approximately $1 billion a year in increased outlays.

We urge Congress to consider reversing or delaying the changes legislated in the 1983 Amendments to Social Security. It would certainly be unwise and premature to implement further modifications in the social security earnings test without first undertaking a serious assessment of the costs and the benefits.

FIGURE 1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME

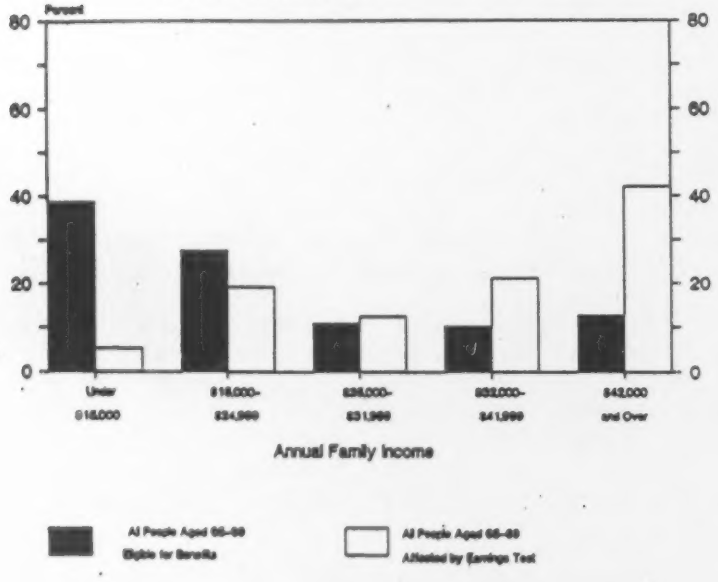
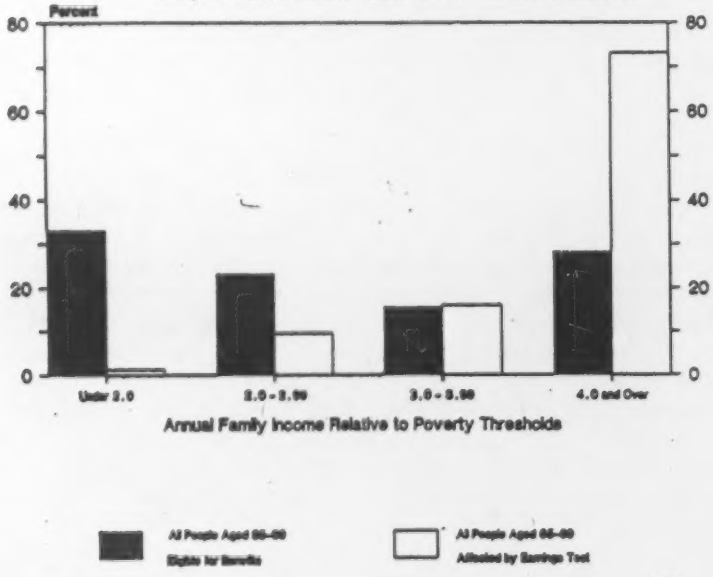


FIGURE 2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

Chairman JACOBS. Ms. Costello.
Mr. POLLACK. She is a resource person.
Chairman JACOBS. You are a resource person.
Mr. Daub.
Mr. DAUB. Thank you, Mr. Chairman.

For all of you, if I had been an employer and I employ a person for 20 years and he is reaching 65, I am not paying that person at the rate of $3.35 any more. I have had him on my payroll for 20 years now and he is pensioned and has gotten a track record with my business that obviously has him around. I don't know that there are very many people that have been employed throughout their whole life. There are some probably, but there are still very few.

I don't think Burger King and McDonalds are paying senior citizens $3.35 to work in most cities in our country. But what I am thinking about is—I know this was true in my case, so it is a personal experience as personnel manager in a company that had 600 people that I wanted that older person who had been trained and was productive to stay on. The problem was he could only work half time to stay under the earnings limit as a general proposition. It has gone up each year.

So my problem was that I could not justify keeping him at half time. I had to have two people. Now, I don't think we want to continue to justify the earnings limitation as labor protection, which might have been one of its original reasons. We had all these young people coming in. We want to make room for them, so this was one way of kicking out people on the older end so the young people could get a job. I don't think we want to continue to argue we need to make room because the labor force is expanding. It is not. It is shrinking, and it is going to shrink even more in the nineties.

So if labor protection or job opportunity is not the reason, then what I worry about is the two-income family, the truck driver, the teamster in my district who is making over the $45,000 limit on the maximum FICA. I have got lots of truckers in my district that are certainly over that—then I can't justify with insurance and liability insurance or anything else only have them drive 20 hours. I have got to go get somebody who will work full time. It is just not efficient to have them half time.

So as I look dynamically—I think, Mr. Pollack, what you said—look dynamically ahead, I also just have a policy question in my mind. I am not sure of why somebody who is making $50,000 and collecting Social Security at age 70 is any different than somebody making $50,000 a year at age 67 or age 66, and not collecting their full Social Security.

Mr. POLLACK. A couple of points. One, I am not sure there is a clear rational ground for having that break at age 70. I am not going to defend that.

Mr. DAUB. You wouldn't suggest we go to 75, would you, as I said earlier a couple of times?

Mr. POLLACK. I am not clear why we don't have an earnings test throughout.

Mr. DAUB. For everything?

Mr. POLLACK. Yes. I think that is consistent.

Mr. DAUB. That is thoughtful.

Mr. POLLACK. Again, I don't think Congress is going to do that. I don't have any illusion about that, but I don't see any particular rational ground for 70. It is a political choice.

Now, I start from the proposition that every single person in this room is really anxious to increase the productivity of the senior population, for many different reasons. It will be helpful to society and it will be helpful to seniors just in terms of their psychic, spiritual benefits. Their health certainly is likely to be improved by being useful, productive, and feeling needed. That is not the question any of us need to differ about.

The question is: What is the cost and the benefit that we achieve through this means of achieving that end?

I submit to you that a good cost/benefit analysis would demonstrate that we are really not spending our dollars well in achieving that end.

Let's take a look at different groups in the population. For the lowest income population, they are not likely to be affected by what we do here. Certainly their income right now is well below the earnings test limit and they have had an intermittent history of involvement in the labor market. They have had difficulties because of educational level, health and so on. Their circumstances are not likely to be changed significantly.

Similarly, those folks at the upper income level are not going to be impacted very significantly.

Let's take a look at the changes that are about to go into effect in 1990. We are saying for all of those upper income folks, instead of having a benefit reduction rate of $1 for every $2 earned, now there is going to be a benefit reduction of $1 for every $3 earned. Now, the Government is going to be spending substantially more money out of the trust fund in order to make that payment, but the behavior of those people is not going to be changed very significantly. It probably will not change at all. I don't think that is a good expenditure, because we are not achieving objectives that all of us agree we would like to achieve.

Now, there is a question of those people at the more moderate income levels that I think all of us really want to focus our attention on. It appears that the data that we have to date is at best questionable as to the impact of changes in the earnings test on beneficiaries' labor market behavior. Certainly we can say there are going to be some people who will increase their hours of work and some who are going to look for work who might not look for it otherwise. There is no question that that is true for some people.

The question is how many will change their behavior and how many will receive benefits without changing their behavior at all?

I think unless we can answer those questions, we don't really know what we are getting for that dollar of expenditure. We know that we are doing something that we think is leading us toward a very commendable goal, but we are not sure of that. I would suggest that before we make that leap, either by eliminating the earnings test or increasing the earnings limit, we need to know a whole lot more in terms of what its impact is going to be in terms of older people's participation in the job market. Without that, I don't think we should make that expenditure.

Mr. DAUB. You could well be right, and I think it is something, as we make public policy in this particular area. Again, I admit I am looking ahead in some crystal ball way, in a way that says we didn't see Alzheimer's disease because our life expectancy was 47, but we knew about because it was depicted on the caves. We are living longer so we see more of that.

We have got a society that is going to see my generation at age 60 with one or both parents alive at age 90. We didn't see that 20 years ago. We are going to see a doubling of the elderly population by the year 2010 or 2020—in that timeframe—there are going to be some people healthy, wanting to work, and this kind of a distinction in the law will get more and more pressure for change.

So I don't know whether it gets done next year or 2 years from now, or 5 years from now, but as those elderly numbers grow, and clearly therefore will be a bigger part of the work force under any circumstances, these kinds of limitations on anybody's earnings are going to become more and more of a concern to the Congress, just as the discriminatory aspect of age 65 and age 70 in the Federal service was.

So I am just saying to you, I can't say statistically that there is as much evidence as I would like to make this change. But I would like Congress, for a change, to be able to look forward to having a change when it is not at the cliff, when it has to be made. It took 24 years to raise the retirement age to 67. Maybe this change ought to be done over a long period of time, over the next 8 to 15 years.

Mr. POLLACK. The next time we look at this issue I think we should feel confident that the expenditure would produce a significant change. If it would not, if we don't have some real confidence that it is going to make that change, I don't think it is advisable to leave it.

Mr. DAUB. Your point is made for the record and your testimony was thoughtful.

I appreciate the AARP testimony particularly. Of course, I am concerned about my teamsters and my bricklayers and my steeplejacks in Nebraska who are retired members of organized labor. Your group is particularly organized labor retirees who are making over $45,000 a year right now and their employers are telling you I can't employ workers at 65 any more because I have got to put them on part time and I can't manage that. I have got to have a full time worker, and that guy doesn't want to work for half of what he was making when he was 65, he wants to get all of what he was making when he was 65.

It is a problem that may not be so bad now, but it is going to grow as the years go by.

Ms. MCKENNA. Mr. Daub, I would like to respond to your question. As far as the members of our group, we have many members of the National Council who are not members of organized labor and we know many of them do not have the high incomes that many of the union people have. But one concern we have—and I will say I agree with most of what Ron Pollack says—but, as far as older people go, and you are posing the question about older employees who you have found valuable and you would like to keep them working, it is our finding that many older people would like

an opportunity for part time work. They are really ready for part time work.

They don't want to separate themselves completely from the work force, and studies have shown for their physical, mental and spiritual health—which was mentioned by Dr. Flemming—it is better for older people to stay involved. But very often they don't have the physical stamina to work that 40-hour week. So the best answer then for everybody, for all concerned, is for part time work, which helps the employer and helps the older person, because the employer is still able to get the skills that have been built up in all those working years and the employee is able to keep earning some money, and also maintain the skills that are necessary to the employer.

We are very concerned about so many of the older people who are working right now at minimum wages. The National Council of Senior Citizens is one of the national contractors of the title V program, so we are familiar with the need of older people for jobs, and we know that many of them then move into jobs in the community. That is the whole goal of the title V program, to get them off of subsidized work.

Many of these people will take the jobs at minimum wage. They are happy to take them. That is all they can get. So there is very definitely this need on the part of older people for work. I think it is a very, very sad thing, a sad commentary that there is this great need, but it happens to be true.

Mr. DAUB. I want to agree now and say what I am trying to do is to take away artificial distinctions, whether it is age or economic circumstances. There are the people that you describe, I agree with you, your comment is thoughtful. I don't want you to misunderstand that I am saying what this limitation or phase out might do is be good for everybody. When we do things like CODA clauses and the high five instead of the high three, we are looking at that seasoned employee in their last year making more than we have given them the benefit for—particularly for females who up until 10 years ago weren't competitive in the work force, so that if the predeceasing spouse was the male, you really got a terrible problem. We did a little bit of adjusting in the 1983 reforms but not near as much as we should have, in my opinion.

I accept what you are saying. It is not a black and white thing with me and I think you make a good point. I am just concerned there are many, many more people who have labored as opposed to have been lawyers or whatever, who I think have earnings that are higher now than people realize and who are going to be affected.

I was a personnel manager. In my particular company we made cattle and hog feed for farmers. I couldn't use the part-time worker effectively in my business and compete with my competitors. I wanted to keep them, but to have job sharing two for ones and all the other things that go with it, was difficult. Not that that isn't a good idea for some businesses, and we are seeing job sharing and a lot of things now that provide opportunity for older Americans in the work place. We need to do more of that. It is just a problem of trying to work out what policy ought to be.

It is not the Government's money in that trust fund. The money that is in that fund is the workers money.

Ms. McCauley.

Ms. MCCAULEY. I would like to add another group of people to your list that you mentioned, Congressman Daub. That is editors, teachers. The teachers work until 65 or 70 perhaps now. However, they are usually discouraged from working that long because they have reached the plateau of a higher wage and with the budgets of the school districts going down, they try to get rid of the people who are in a higher wage bracket even though it isn't terribly high. It saves them money, but it does lose very good editors, very good teachers, but they are out and injured. They are released.

Mr. DAUB. Buyouts are going on in public and private industry where they are buying out the older workers sooner. Remember, the company has got to pay the FICA match. One half of this is paid out of the corporate gross. It is adjustable but it is taken out.

I appreciate the dialogue, Mr. Chairman. This has been helpful.

Chairman JACOBS. Me, too.

I have a couple of observations. One is Ms. McCauley, the teacher who is denied her or his livelihood by the school board certainly isn't involved in the issue before this committee.

Ms. MCCAULEY. No, no, that is true. I was merely including employment——

Chairman JACOBS. She can't use any more earnings. The earnings test doesn't help her very much.

Ms. MCCAULEY. I was just adding to Mr. Daub's point of age discrimination in employment—when people are forced out of the work force possibly because employers do not want to pay higher wages, as small as they might be.

Chairman JACOBS. The other point I think I would like to put on the record is that your $42,000 bricklayer certainly doesn't have to retire when he is 65 years of age. He can go ahead and maybe his choice is between $12,000 Social Security benefit and a $42,000 salary.

Mr. DAUB. He has a pension too, probably.

Chairman JACOBS. That too. But however that might be, the one point I would like to imprint upon the record is that there is no Social Security law in the United States that says a person cannot work past the age of 65. It simply says that you cannot work and pretend you are retired at the same time past the age of 65. That is the point that I think ought to be on the record.

Mr. DAUB. Would the gentleman yield on that point?

Chairman JACOBS. Sure.

Mr. DAUB. Unless you are able to get to age 70 and then it is OK.

Chairman JACOBS. Yes, but this gentleman indicates his district voted against repealing the retirement test at the age of 70.

Mr. DAUB. I know. My colleague has always been consistent.

Chairman JACOBS. As a matter of fact, my old friend, David Stockperson was testifying about that before our committee.

Mr. DAUB. You have the professor with their tenured contracts. They didn't want it either.

Chairman JACOBS. When we got down to that point, the same year the administration wanted to, I say, virtually, if not virtually, eliminate retirement at 62 by reducing the benefit from the 80 percent of full benefit to 55 percent of full benefit, and that was to take place January 1, 1983. That was just right now. The U.S.

Senate voted in opposition to the idea 100 percent to zip before it ever got there. They adopted a resolution saying don't bother to extend it. That was bipartisan, 100 percent.

So at the same time the proposal was to reduce the benefits for some bricklayers whose backs didn't feel very good any more after age 62, and arguably had more reason to retire than lawyers at age 62, they were proposing liberalization of benefits for people all the way up to Lee Iacocca. Maybe even television ministers, I don't know, but way up there in the big bucks.

And so I asked Mr. Stockman, let's see now, at the same time you are asking to cut the benefits for the fellow who maybe worked out digging ditches, you are asking to increase benefits which would include people who can command incomes of a couple—$100,000 a year. How do you square that?

And Dave said, well, Congressman Jacobs, you and I have many times discussed the thin line between earned incomes and unearned income.

Then I said, well, let's just take a couple of cases. A lawyer who can make $100,000 a year, if your proposal passes, suddenly gets so-called golf cart money, doesn't he? Suddenly he gets $12,000 a year more gratis, or at least according to what the law is now.

Let's take a President who is about to be 70 years old and gets $200,000 a year, suddenly would have a $12,000 manna from Uncle Sam.

That is when Dave repeated. He said there is a thin line between earned and unearned income.

I said, well, is there any doubt in our mind about whether this President is earning his income? And at that point I don't think we penalized the people at 62 or added to the luscious life style of those older people commanding high salaries.

Mr. DAUB. I think we should make a distinction it is OK after age 70 but not at 65. I think that is the problem.

Chairman JACOBS. I agree with Mr. Pollack. I think if you are making $500,000 a year, that should be a gentle sufficiency even if you are as old as Methuselah.

We thank the panel.

Mr. DAUB. Thank you very much.

Chairman JACOBS. Our final panel today consists of the National Federation of the Blind, Mr. Gashel, an old friend, and National Committee To Preserve Social Security and Medicare, William Lessard.

Mr. Gashel, I believe you are first.

Mr. GASHEL. Thank you, Mr. Chairman.

STATEMENT OF JAMES GASHEL, DIRECTOR OF GOVERNMENTAL AFFAIRS, NATIONAL FEDERATION OF THE BLIND

Mr. GASHEL. The National Federation of the Blind has had a historically strong and substantial interest in the whole area of Social Security programs. It is a pleasure to testify today in this hearing.

We know firsthand the human and economic needs of blind persons and particularly the need to improve work incentives in the Social Security programs. We have been telling the Congress about

this for a number of years, and you have been quite helpful in a number of instances.

Now, in this hearing today we are really examining operations for modifying the Social Security retirement test. It has been proposed, and we actually agree with that, that the retirement test should be eliminated altogether.

The retirement test is only a limitation on earnings for individuals who are qualified for Social Security benefits were it not for their earnings. The retirement test is not a limitation on wealth. Even the very rich qualify for Social Security and receive it just as long as they don't work too much.

When we think about the retirement test and the possibility that it may be modified, Congress would also have to consider what impact this may have on blind beneficiaries of all ages. Provisions of the Social Security Act have forged a link between the limitations on earnings of the blind who have not yet attained age 65 and retirees, blind or not, who are age 65 through 69. Changing the law then with respect to these retirees will raise the question of how earnings for blind persons of all ages should be treated.

To examine this question, let's take a look at the total population of the blind, as a whole. I will give you a little profile on that.

Consider the blind person who is age 70 and older. Now, that person has the absolute maximum incentive to work, but few people at that age, and especially people who are blind, can do so. So the incentive doesn't really mean very much in Social Security and economic terms, certainly, although it means something to some individuals. There is no limitation on earnings at that age.

Now, then we come to the blind individual who is age 65 through 69. There is a little bit more incentive to work. There is, of course, the earnings limitation, but it is set off by the provisions of paragraph 203(f)(3), which do permit the individual to work some and only gradually lose Social Security benefits, and that provision will be liberalized a little bit more in 1990. So there is some more incentive to work.

Again, this is not the largest segment of the blind population who could work. When we get to that segment, those blind people who are between the ages of 18 and 65, we find that there is a tremendous disincentive to work. The moment a person earns at the same earnings level, the same basic exempt amount under section 203(f)(8), that person is faced with a cliff. Either you earn the next dollar and lose all the Social Security benefits to which you have been entitled, or you forgo earning the next dollar and keep the Social Security benefits.

It is not offering people a very good choice, and it is not a very good social choice, let alone for the individual. It doesn't make good economic sense.

Now, in my written statement I have explained the basis for the linkage between the group of retirees and blind beneficiaries of all ages. As with retirement, blindness is a defined condition in the Social Security Act. Either you are or you are not. Of the 498,000 people in the United States who are blind within the meaning of the act, 54 percent have attained age 65. With a few exceptions, most of these people are already beneficiaries and they certainly

get more work incentive than the blind people who are under age 65.

If we now add that group, add to the picture of the older or senior blind people, people who are age 65, we find that another 27.5 percent are beneficiaries. So in total we come up to, adding those two populations together, 82 percent of the blind population as a whole that are beneficiaries. An additional 8 percent of the blind population is made up of individuals who are under the age of 18.

This really leads to the bottom-line conclusion that less than 10 percent of the blind population in this country work. Most do not work, and most are Social Security beneficiaries. We know that there are certain social and economic consequences that accompany blindness. Most blind people certainly experience them. Being outside of the work force is a big part of it.

Maintaining an earnings limitation in the case of blind persons of all ages, as well as in the case of retirees, mixes a welfare concept or a means test concept approach with a social insurance program. But Social Security is actually insurance, not welfare. Its benefits are payable to the rich and the poor alike—even the very rich. Wealth, as I said before, doesn't matter in terms of Social Security. It has no bearing on eligibility whatsoever. Only earnings are penalized. This, in the case of blind people, is a very counterproductive and wrong approach.

We think that the principles of insurance should be applied consistently across the board, to the rich and the poor alike, to the working blind and the nonworking blind. In fact, we think work should be encouraged.

Now, just a final word on a couple of demographics here.

In economic terms, Social Security removing the earnings limitation which now applies to all blind beneficiaries would increase the beneficiary rolls only by a minuscule fraction. It would add something like 30,000 to 40,000 beneficiaries to the rolls.

The payoff from the point of view of the Social Security system would be the newly generated revenues resulting from the maximum work incentive being shifted to approximately 130,000 blind persons and their dependents who are of working age and who could work if they were offered an incentive to do so.

For the most part, these individuals are now beneficiaries. They are not working and they are not paying Social Security taxes.

Mr. Chairman, I am going to cease at that. I am going to thank you for hearing our statement today and allowing us to participate in a very meaningful hearing.

Chairman JACOBS. Thank you, Mr. Gashel.

[The statement of Mr. Gashel follows:]

BEFORE THE SUBCOMMITTEE ON SOCIAL SECURITY

COMMITTEE ON WAYS AND MEANS

UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, D. C.

STATEMENT OF THE

NATIONAL FEDERATION OF THE BLIND

JAMES GASHEL

DIRECTOR OF GOVERNMENTAL AFFAIRS

SEPTEMBER 29, 1988

Mr. Chairman, I am James Gashel. I am Director of Governmental Affairs for the National Federation of the Blind (NFB). My address is 1800 Johnson Street, Baltimore, Maryland 21230. Thank you for offering me this opportunity to present the views of the NFB in response to the Social Security Subcommittee's interest in reviewing options for modifying the retirement test.

There are over fifty thousand blind people who are members of the National Federation of the Blind. We have a local chapter of the Federation in almost every sizable population area in this country and a state affiliate in all states and the District of Columbia. In short, Mr. Chairman, NFB is organized and active in all parts of the United States.

By virtue of its size and scope NFB represents and speaks for the blind as a collective body--we speak for older blind persons and younger blind persons, as well. The positions we express in hearings such as these are the result of the

democratic process of debate and decision making. The supreme authority of the Federation is its national convention, which occurs annually. During the convention we openly debate (and approve or disapprove) a number of policy resolutions. In this manner the Federation is truly the blind speaking for themselves. It is not simply an organization speaking for the blind. All of our elected officers and the vast majority of our members are blind. For these reasons the NFB is widely known as the voice of the nation's blind.

This hearing concerns the Social Security retirement test and various approaches that may be taken to modify it. Blind people have a special concern in relationship to this subject. Most blind people are age 65 or older. The National Society to Prevent Blindness has estimated that there are 265,950 blind retirees (age 65 or older) in this country. According to the same data there are 498,000 blind persons (of all ages) who meet the Social Security Act's definition of blindness.

The retirement test affects blind retirees in much the same way that it affects all senior citizens aged 65 to 69. But the retirement test also affects other blind people who receive Social Security benefits but have not yet attained age 65. This latter group is made up of about 85,000 blind "disabled worker" beneficiaries. Under a provision in section 223(d)(4) of the Social Security Act, these individuals are subject to a test of "substantial gainful activity" which exempts average monthly earnings that do not exceed the "exempt amount" for Social Security retirees under section 203(f)(8) of the Act. The amount of allowed earnings under this section is currently $700.00 per

month, subject to upward adjustment in January, 1989, and at the beginning of each succeeding calendar year. Unlike other individuals described in section 203(f)(8), blind individuals who have not attained age 65 are not subject to the "excess earnings" principles of section 203(f)(3). So for these individuals the "exempt amount" of $700.00 is an absolute earnings limit.

These facts about the blind population in general and its relationship to Social Security indicate that blind beneficiaries of all ages are likely to be affected by any changes that Congress may make in the retirement test. Certainly the majority of blind individuals would be affected as retirees. Those who are not yet retirees, but are subject to the same basic "exempt amount," would also be affected in some way if Congress decides to raise the retirement age or to eliminate the retirement test altogether.

Keeping this background in mind, it is our considered position that Congress should maintain the rationale of a linkage between blindness, as a defined disability, and attainment of age 65, as the legally defined age of retirement. The test of "substantial gainful activity" (SGA) is used to determine the presence of a disability (for individuals who are not blind) under Social Security regulations. Evaluations of both earnings and the extent of work activity are the measures of SGA for a disabled individual. This is also true in the SSI (Supplemental Security Income) program (for the disabled but not the blind), since SGA is the central measurement of the existence of a disability.

SGA is not employed as a measurement tool to define the

existence of a disability in the case of the blind, however. This is true for all blind individuals under age 65, whether they receive disability insurance or SSI benefits. The only test that is actually applied to regulate work activity of blind disabled workers is the "exempt amount" under sections 223(d)(4) and 203 (f)(8). In fact, when earnings of a blind beneficiary exceed this "exempt amount," the disability (blindness) is determined to be "continuing." In the language of Social Security, the blind individual who works continues to maintain a "period of disability" but may not be entitled to cash benefits due to average monthly earnings that exceed the "exempt amount." I should underscore once again that under SSI there is no test of SGA used to define the presence of a disability for individuals who are already defined by law as "blind."

Thus the present posture of the law tends to align the treatment of earnings of blind beneficiaries (under age 65) with the treatment of earnings of all retirees (blind or not) aged 65 to 69. Treatment of earnings for the blind is more closely aligned to treatment of earnings for retirees than it is to treatment of earnings for disabled beneficiaries who are not blind. This alignment is appropriate and should continue if the retirement test is modified.

Treating the blind as "disabled" by using the SGA test would be inappropriate. Blindness is a defined and detectable physical condition with predictable economic and social consequences that flow from it. Blindness is, in fact, the only physical impairment that is actually defined in the Social Security Act. Identification of blindness in conformity with this definition

can be made quite reliably by an ophthalmological examination. These facts are important to understand in evaluating the validity of applying the SGA concept.

SGA is generally a measurement tool that is used to define disabilities other than blindness. Thus, in Social Security terminology, a person is "not disabled" if he or she has demonstrated an ability to engage in (or is actually engaging in) SGA. On the other hand, the person is "determined to be under a disability" if he or she cannot perform SGA.

In blindness cases, however, SGA measurements tell us nothing about the existence (or absence) of disability. The disability in these cases is determined by applying the definition in the Act. The only effect of the SGA measurement in SSDI blindness cases is to limit work activity of blind persons. That in our view is a totally counterproductive use of the SGA concept.

In SSI blindness cases, on the other hand, SGA is not applied. Income of blind persons eligible for SSI is, of course, limited by income restrictions of SSI unrelated to the definition of disability. But a measurement of "Substantial Gainful Activity" in blind SSI cases is not a factor whatsoever. That is an entirely appropriate way to handle the determination of blindness. The fact is, that as the Social Security Act accurately recognizes, blindness exists as a particular physical condition regardless of SGA.

If the SGA test should not be applied to the blind (as it is not applied currently), how should earnings of the blind be treated? This question brings me back to the matter of the

retirement test. Earnings of the blind (retired or disabled) are now subject to the same basic "exempt amount." As with retirees (blind or not), the "exempt amount" is actually an earnings limitation. Mr. Chairman, it is our considered position that this earnings limitation should be removed for all individuals subject to section 203(f)(8), including blind individuals of all ages. Here is the rationale for this position.

Blindness as we still experience it today has profoundly adverse social and economic consequences. Therefore, Social Security benefits should offset these consequences insofar as possible. The social attitudes about blindness are full of myths and misconceptions. As a group, the blind face an incredibly devastating set of artificial impediments when they seek to enter and compete in the labor force. The blind are not just viewed as unemployed. We are usually considered unemployable.

To be sure, the blind pay a heavy price for this erroneous labeling. For example, most people agree that over seventy percent of the employable blind population is either unemployed or underemployed. If before blindness an individual had an income of, say, fifteen thousand dollars annually (not an uncommon income for sighted individuals), and if after blindness that same individual finds employment at $8,500.00 annually (not at all an uncommon experience for the blind), he or she will still not be eligible to continue receiving full Social Security benefits despite the fact that a substantial loss of income has occurred. Blind individuals who have not attained age 65 would not be entitled to benefits at all in the circumstances just described.

Under the present conditions prevailing in our society the blind are required to suffer the indignity of being cast aside in competition for jobs and social opportunities, and we are also required to pay in terms of cold cash for our second-class status. The social attitudes about blindness which have traditionally prevented us from assuming the more responsible positions and holding the more lucrative jobs in the labor force have been fostered by society as a whole, not just by the blind members of society. In fact, these attitudes have not principally been fostered by the blind at all. Therefore it is equitable for us to propose that everyone should share in carrying the financial burden imposed on us by these social attitudes--a burden which we now bear alone.

Another set of economic consequences facing the blind is the result of the Social Security system itself. I refer here to the disincentive factor which inhibits the initiative of any blind person who is naturally concerned about some degree of long-range economic security. The economic realities are these: under existing law, if an individual becomes blind and has average monthly earnings which do not exceed the "exempt amount," he or she will likely draw full Social Security benefits. The individual has every incentive to remain unemployed and not return to work at all. Why? In the first place, he or she is probably not an expert in the law. The law is complex, and the talk of allowed earnings, trial work periods, and the like is confusing and not generally conducive to an attempt to resume or continue working.

The penalties for working are even greater for blind individuals who have not yet attained age 65. If the individual goes to work and (after a specified trial work period) is earning somewhere in the neighborhood of $700.00 per month, benefits will be terminated abruptly. Ironically, earnings of a blind individual have a much less dramatic effect on benefits upon attainment of age 65 and no effect whatsoever when the individual reaches age 69. Blind persons under age 65 with dependents may in some instances receive over $1,500.00 per month, the current family maximum. All of this will be lost when earnings exceed 700.00 per month. The individual with very modest earnings of $800.00 or $900.00 per month (or even more) is penalized for having tried to become self-supporting.

Place yourself in the position of a blind person considering possible employment. Remember that, including dependents' benefits, the family income from Social Security may exceed $1,500.00 per month. I know a number of blind people who (believing in the work ethic) would accept employment offering gross wages at somewhat less than their possible Social Security income. They must, however, also consider deductions for income and Social Security taxes, as well as a variety of expenses related to their work. Commonly a blind person finds it necessary to employ a reader or driver, and these expenses lower the take-home pay even more. Facing such circumstances, can a blind person afford to take a job at the risk of economic security? Some think they can, but many have found that they simply cannot.

Retirees and blind individuals of all ages should become entitled to Social Security benefits after performing a certain amount of covered work. The basis upon which this should be adopted is the broader social benefit which would result if an entire segment of the population whose talents are now underutilized were to be made fully productive. Under this proposal the blind beneficiary of any age would know that he or she could count on a monthly insurance payment. It would not be jeopardized by attempted work. The blind person is better off (and society generally is better off) for the person to be productive instead of idle--working instead of sitting at home.

Proposals to eliminate the earnings limitation have traditionally misapplied a welfare concept to Social Security, which is not welfare. For example, proponents of the earnings limitation complained that individuals with high earnings would continue to receive their Social Security benefits. But the fact is that the number of blind people being paid say $30,000 or more annually is very small. Most blind people do not even work.

In the case of the blind, consider how the work incentives in Social Security are really out of focus with the work capability of blind people. More than half of the blind population is aged 65 or older. Many have worked enough (especially as sighted people) to be qualified for Social Security retirement benefits. These older blind people (who are mostly outside of the workforce) have a greater work incentive than do the blind who are between the ages of 18 and 65. This is because of the treatment of excess earnings under section 203(f)(3).

Once a blind person reaches age 69 (as in the case of all retirees), the work incentive actually increases. At that time the limitation on earnings is removed altogether. This means that the few blind people who can still work at age 69 or older can earn to their heart's content even if they are earning over $30,000. Meanwhile, their blind counterparts aged 64 and below are limited to earning no more than $700.00 per month. Many of these people could actually work more (subject to job availability) if they had the same work incentive as their blind counterparts at age 69 or older. But the fact is that these younger blind people are actually being paid to stay outside of the workforce. This approach is wrong.

Removing the earnings limitation could add an estimated 30,000 to 40,000 blind individuals to the beneficiary rolls. The payoff (from the income side of the Social Security system) is the maximum work incentive that will be aimed at the blind of all ages who now receive any type of Social Security benefit. Fewer blind individuals would receive SSI as a result of becoming Social Security beneficiaries. There would actually be a positive cost impact on the Social Security system resulting from increased payments into the trust funds by those who are now beneficiaries. The greater their earnings, the greater will be the amount that they pay into the trust funds. We estimate, conservatively, that as many as 130,000 blind beneficiaries of all ages and their dependents will receive an added work incentive by the earnings limitation removal. Then the benefits they receive will be offset in part by the taxes they will pay. Now they only receive benefits and do not pay Social Security

taxes in most instances.

Mr. Chairman, in concluding this testimony, I would like to restate and reemphasize the message that we have been giving to this subcommittee and the Congress for several years. The blind as a group are prepared to work and work hard. The legislation which we recommend to your attention constitutes an effort on our part to renounce our traditionally established lives of demeaning dependency and subordinate status. In asking for work incentive legislation we express our firm determination to escape from many long decades of custodialism during which we have been constrained by society's ignorance, myths, and misconceptions. We seek to free ourselves from the captivity of ignorance, prejudice, and discrimination. We ask only the opportunity to lead normal, self-supporting, independent lives. For our part, Mr. Chairman, we are committed to use work incentives effectively as instruments of rehabilitation, self-help, and self-support for the blind. On behalf of the National Federation of the Blind, I thank you.

Chairman JACOBS. Mr. Lessard.

STATEMENT OF WILLIAM J. LESSARD, JR., DIRECTOR OF POLICY AND RESEARCH, NATIONAL COMMITTEE TO PRESERVE SOCIAL SECURITY AND MEDICARE

Mr. LESSARD. Mr. Chairman, I want to thank you for your patience sitting through this long day. I am only fueled by one English muffin, so I am sympathetic to your situation going for a whole day.

I am William J. Lessard, Jr., director of policy and research for the National Committee To Preserve Social Security and Medicare. I am pleased to be here today on behalf of our 5 million members and supporters to express the views of the national committee for repeal of the Social Security retirement test. We support repeal for all beneficiaries, regardless of age, including the disabled.

The national committee also supports immediate implementation of equitable delayed retirement credits for all people who remain in the work force after full retirement age and urges extension of DRC's to spouses and working widows.

What are our reasons for this position? The national committee opposes the retirement test because the high "marginal tax rate"—I use that in quotes—discourages healthy, energetic older individuals from remaining in the work force.

As you know, the national committee has also opposed provisions that are work disincentives in the Social Security disability program. We think work is a value and that Americans value work highly.

The national committee opposes the retirement test because it locks into poverty widows, workers in poor health and the underemployed who must apply early for benefits because limited income does not permit the luxury of waiting to receive unreduced benefits.

The national committee opposes the retirement test because it strips younger families of the full value of the Social Security survivor benefits purchased with Social Security taxes paid by the deceased worker.

In my written statement I cite numerous letters from national committee members who describe better than I can how the retirement test is a disincentive to work, is not fair and is very confusing.

I will just refer to a few excerpts. Mrs. Esther Buell from Shawnee, Kansas, writes, "The system makes liars and crooks of the population who have to draw Social Security and still work to survive. I want to work. It is depressing to know that I can't survive on Social Security alone and what I'm allowed to make."

To a widow from Laurens, South Carolina, the retirement test penalizes her for responding to the critical need for her services at her local hospital. She writes, "We have people who won't work and help out because the Government takes too much of the overpayment. The wages is not a lot of money. Why keep a person down to a low income?"

A member from Andover, Massachusetts, also asks, "Would someone please give me a reasonable answer as to why there is a

cap on earned income? The organization I work for on an 'on call' basis would like me to work more, but the Social Security hassle dictated that I should decline."

These are only anecdotes, but we think that reinforces the dynamic situation that Congressman Daub has talked about, that there are individuals out there who want to work and who just feel burdened by the program.

If Congress wants to keep some retirement test because of the short-term cost, the earnings limit should be the same for all beneficiaries.

Congressman Ron Wyden recommends equalizing the earnings limitation for those over and under 65. Gradually over the next 10 years his bill would approximately double the earnings limit. According to CBO, doubling the earnings limit as in Congressman Wyden's bill would exempt nearly half of all affected beneficiaries from the retirement test, completely exempting most women, widows and widowers and people with low family incomes. This study makes us believe that the Wyden approach to phasing out the retirement test may be the best approach.

One hardship frequently overlooked involves overpayments, the majority of which are related to the retirement test. While SSA will waive repayment if a beneficiary is poor and without fault, SSA does not consider confusion about the retirement test an adequate excuse. SSA has estimated 80 percent of beneficiaries affected by the retirement test have retroactive corrections of benefits. This is evidence that many beneficiaries, the majority, simply do not understand how the retirement test works, especially in the first year. Repealing the retirement test would eliminate the resulting overpayment hardship.

Opponents of retirement test repeal apparently object that upper-income individuals would benefit the most, but Social Security is an insurance program. Why shouldn't all individuals, rich and poor alike, collect the benefits they have paid for?

Congressman Archer's proposal to phase out the retirement test for those over age 65 also has merit, but the key contribution of his legislation is that it restores a better balance between equity and adequacy by immediately making the delayed retirement credit actuarily fair.

Upper-income workers have the lowest rate of return on their Social Security contributions and half of those benefits are now taxed. To apply the retirement test on top of that, without an equitable delayed retirement credit, is unfair. While early retirement reductions currently are generally fair, the delayed retirement credit will only be actuarily fair in the next century.

As regards the contract that you referred to earlier, Mr. Chairman, Congress has already made that decision to change the contract in terms of the delayed retirement credit to make it actuarily fair. Congressman Archer's bill would only accelerate it. When the delayed retirement credit is made actuarily fair, it then makes no sense not to give workers a choice between reduced benefits at early retirement age or increased benefits later. The beneficiary will receive no more total money than he does currently and the Social Security fund will pay out no more money than it would if we hadn't given that choice.

We strongly urge the subcommittee to also assure that widows who work past retirement age receive increased benefits for delaying retirement. As it is, most widows do not receive higher benefits even if they work past retirement age. To address this problem, the national committee has developed a working widow protection proposal, which we have already shared with subcommittee staff.

The national committee hopes the subcommittee will respond favorably to the desires of seniors to keep working by eliminating or reducing the retirement test and making fair adjustments for delayed retirement.

In closing, I would like to add that one advantage of testifying last is the opportunity to think about responses to questions posed to earlier witnesses. Earlier, Mr. Chairman, you asked Commissioner Hardy what we would call benefits if we eliminated the retirement test, since they are generally called retirement benefits now. But the current name for the Social Security program is the Old Age and Survivors Insurance.

Chairman JACOBS. She made that point.

Mr. LESSARD. I think that would be very adequate. We wouldn't have to change anything.

Thank you very much.

[The statement of Mr. Lessard follows:]

NATIONAL COMMITTEE TO PRESERVE
SOCIAL SECURITY AND MEDICARE

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STATEMENT OF
WILLIAM J. LESSARD, JR.
REPRESENTING THE

NATIONAL COMMITTEE TO PRESERVE
SOCIAL SECURITY AND MEDICARE

PRESENTED TO THE

SUBCOMMITTEE ON SOCIAL SECURITY
COMMITTEE ON WAYS AND MEANS
U. S. HOUSE OF REPRESENTATIVES

REGARDING

THE SOCIAL SECURITY RETIREMENT TEST

SEPTEMBER 29, 1988

I am William J. Lessard, Jr., Director of Policy and Research for the National Committee to Preserve Social Security and Medicare. I am pleased to be here today on behalf of our five million members and supporters to express the views of the National Committee with regard to the Social Security retirement test.

The National Committee supports complete repeal of the Social Security earnings limitation or retirement test - not just for those over age 65, but for all beneficiaries, regardless of age. If Congress is not willing to repeal the retirement test immediately because of the short-term cost, then -- at the very least -- today's low limits should be raised.

The National Committee also supports immediate implementation of equitable delayed retirement credits (DRCs) for all workers who remain in the work force after full retirement age and urges extension of DRCs to spouses and working widows.

Over the long term, abolishing the earnings limitation is cost neutral if early retirement reductions and DRCs are both actuarially fair. Congress has already agreed to make DRCs equitable, but under present law, equity will not be achieved for another 20 years.

The retirement test discourages healthy, energetic older individuals from remaining in the work force because the marginal tax rate on their earnings is too high and DRCs do not begin to compensate for delaying benefits.

The retirement test, by offsetting 50 cents for every dollar of excess earnings, locks into poverty the underemployed, workers in poor health and widows who apply for early retirement benefits because they have no choice. Limited ability to earn income does not afford them the luxury of waiting until full retirement age to receive unreduced benefits.

The retirement test strips younger families of the full value of the Social Security survivor benefits purchased with Social Security taxes paid by the deceased worker. All across this country, both parents frequently work because it takes two incomes to adequately house, feed, clothe and educate a family. But when one parent dies, Social Security protection can be lost to the family if the surviving parent or even one of the children earns more than a minimal income.

Mr. Chairman, we have to ask. Should we be discouraging any segment of our population from contributing their skills and productivity to our economy? We believe the answer is no. Are these restrictions not contrary to the very work ethic this country espouses? The National Committee believes the answer is yes.

If there is an earnings limit, it should be the same for all beneficiaries. No less an authority than former Social Security Commissioner Robert Ball, in his 1978 book *Social Security Today and Tomorrow*, forecast the confusion and the inequity which have resulted:

> "One change in the 1977 amendments -- allowing different exempt amounts for those 65 and for those below 65 -- will greatly complicate the explanation of the test, and, moreover, I see no basis in equity for the distinction. I would apply the over-age-65 test that is in present law to workers of all ages."

Congressman Ron Wyden recommends equalizing the earnings limitation for those over and under 65 and then proposes raising the limit by $1,000 per year over the automatic adjustment in current law. Within ten years, the limit would approximately double and would roughly equal average earnings in the economy.

The Congressional Budget Office (CBO) study, which this Subcommittee requested, found that doubling the earnings limit would exempt nearly half of all affected beneficiaries from the earnings limitation. According to CBO:

> "Among those affected by the earnings test, most women, widows and widowers, and people with low family incomes would become exempt if the earnings limit were doubled."

If CBO had also studied those under age 65, we believe the results would have reinforced its conclusion.

What would a gradual rise in the earnings limitation mean to Social Security beneficiaries who want or need to work at least part-time?

To 63 year old Mrs. Esther Buell of Shawnee, Kansas, who has worked ever since she was 18 years old, it would mean the difference between having or not having sufficient income to meet her basic needs. Mrs. Buell did not choose to retire early. She was forced to apply for Social Security when the company for which she worked closed all of its regional offices and she was unable to find a job with a salary sufficient to support herself. Then when she found part-time employment, she earned over the limit and lost $881 in benefits which is being recovered at $25 a month. She writes:

> "I would be delighted to get off SS if I could find a job sufficient to make a living for myself. . . The system makes liars and crooks of the population who have to draw SS and still work to survive. . . I want to work. It is depressing to know that I can't survive on SS alone and what I'm allowed to make. My health insurance costs me $134.48 a month!"

To a widow from Laurens, South Carolina, and to John Goossens of Irvine, California, both 67 years of age, raising the earnings limitation penalizes them for responding to the critical need for their services at their local hospital.

Our member from South Carolina. is trying to set aside earnings now so that she can afford to retire at age 70. She writes:

> "I've worked and made only $1,000 or $2,000 over my allowance and (incurred a) penalty of over $500. I'm needed at the hospital. We have people who won't work and help out because the government takes too much of the overpayment. The wages is not a lot of money. Why keep a person down to a low income."

Mr. Goossens commands a higher income. He points out:

> "As soon as I have reached the $8,400 limit. . . my hourly rate drops to $4.50 because Social Security takes 50% of my gross earnings, while all taxes are still based on gross. It is because the hospital needs my help, otherwise I would stop working."

Each of these cases points up another serious problem, and that is the inadequacy of the explanation or of retiree understanding of the earnings limitation, particularly in the first year of retirement. Misunderstanding frequently results in overpayments. Last week this Subcommittee examined

some of the hardship issues involving overpayments, the majority of which were caused by the retirement test.

Social Security can waive repayment if an individual is without fault and repayment would cause hardship, but confusion over complex earnings limitation rules, as so often is the case, is not an acceptable excuse. The overpaid individual will be "at fault" and, therefore, ineligible for waiver of repayment.

The widow from South Carolina can ill afford forfeiting a full month's benefits. She would not have deliberately risked a penalty by a failure to report her earnings by April 15 had she understood reporting requirements.

Mr. Goossens thought he was entitled to the $8,160 earnings limitation beginning with the first month he received benefits, April, 1987. Thus he was totally unprepared for the overpayment notice that told him by working from October through December and earning $5,880, he forfeited three months of benefits for himself and his wife.

A member from Andover, Massachusetts, was equally confused about the earnings limit in his first year of retirement. If $6,000 was his annual limit when he retired at the end of April, 1986, he reasoned that he was entitled to earn $4,000 in the remaining eight months of the year:

> "Would someone please give me a reasonable answer as to why there is a cap on earned income? Especially the first year. I was only allowed to make $500 a month . . . but because I earned a little over $600 for four months, I had to return $2,500 in benefits. I did not exceed the gross of $4,000 for those eight months.
>
> "The organization I work for on an 'on call' basis would like me to work more, but the SS hassle dictated that I should decline. What is really bad is they want a projected estimate of your income. If it exceeds $6,000 they want to reduce your benefits immediately. A part time or 'on-call' job is not a permanent job. You're paid as you work. For the government to start decreasing your benefits based on an estimate or assumption is unreasonable."

Immediate withholding of benefits also strikes a member from Chicago, Illinois, as unfair. He provided SSA with an honest estimate of earnings slightly above the $8,400 limit. As a result, he wrote:

> "They have withheld a <u>full</u> month's benefit even though the amount I would owe back at the end of the year would be considerably less! Isn't it a shame the way they treat older Americans?"

Our member from Chicago also reported that he was unfairly penalized a full month's benefits for not timely filing a report of earnings in the first year of his retirement. It has been nine months since he filed a request for an administrative law judge hearing on the penalty issue, but he is still waiting for a hearing date.

Processing earnings estimates, overpayments and underpayments is costly as well as administratively burdensome to recipients and SSA alike. And when benefits are withheld because of SSA errors, beneficiaries can be left without essential income. Mr. Frank Reed of Moline, Illinois, filed a notice of non receipt when he did not receive his January Social Security check. Mr. Reed accurately estimate his 1988 earnings as zero when he retired in July 1987. SSA withheld his benefits because they erroneously estimated 1988 earnings equal to Mr. Reed's 1987 pre-retirement earnings.

Only through total elimination of the retirement test will such problems and controversies as those cited above be a thing of the past. Opponents of repeal raise the alarm that upper income individuals would benefit the most. But Social Security is an insurance program. Why shouldn't all individuals, rich and poor alike, collect the benefits they have paid for?

The Social Security benefit formula is meant to be a balance between adequacy and equity. In the pursuit of adequacy, the benefit formula is already designed to provide a higher rate of return to workers with low average lifetime earnings. Upper income workers, on the other hand, have the lowest rate of return on their Social Security contributions on earnings. And half of those benefits are now taxed! To withhold benefits on top of that, without an equitable delayed retirement credit, is unfair.

Congressman Archer's proposal to phase out the retirement test for those over age 65 in five years also has merit, though we believe that any liberalization should also include those under age 65. The key contribution of Congressman Archer's legislation is that it restores a better balance between equity and adequacy by immediately making the DRC actuarially fair. While the early retirement reductions do differ, they are generally fair. If the delayed retirement credit is also made actuarially fair, as recommended by Congressman Archer, it makes no sense not to give workers a choice between reduced benefits at early retirement age or increased benefits later. We believe, however, more informed choices would be made by Social Security beneficiaries if SSA would initiate a public information campaign to help retirees and survivors better understand the benefit implications of early or late retirement.

We strongly urge this Subcommittee to assure that widow(er)s who work past full retirement age receive the benefit of a delayed retirement credit. Because most widows receive higher benefits as widows than as workers, they learn upon retirement that no matter how long they work past retirement age, they will never receive a single extra penny. Delayed retirement credits on their own work records merely reduce widow benefits they would otherwise be entitled to receive. This is unfair and does nothing to encourage widows to remain in the work force. Legislation introduced by Congressman James Oberstar would correct this inequity by applying a delayed retirement credit to the highest benefit for which the widow was eligible -- either her own or her widow benefits.

As a result of the 1977 Social Security Amendments, widows became eligible to receive the extra benefits earned by their husbands who worked past retirement age, but a wife is still not entitled to any portion of her husband's DRC in her spouse benefits. This, too, deserves correction because it dilutes the real value of what is already an inequitable DRC.

Finally, we want to emphasize that CBO did not look at the dynamic economic impact of eliminating the retirement test in terms of increased work effort and taxes. Increased taxes would help to minimize the short-term cost. While admittedly very rough estimates, SSA actuaries concluded that 36 percent of the five year gross cost of the Archer bill would be offset by increased revenues or other adjustments.

The National Committee hopes this Subcommittee will respond favorably to the desires of seniors to keep working by eliminating or reducing the retirement test.

Thank you.

Mr. DAUB. Mr. Chairman, thank you.

I think you make a valid point about upper-income beneficiaries who, according to CBO, would benefit first from elimination of the retirement test: first, that the benefits are weighted so that the upper-income worker—including Congressmen, I might add—some of whom live beyond age 70 and continue to draw $89,500—get the least return on the FICA taxes paid, if you look at it; second, that those are the beneficiaries most likely to pay income taxes on benefits, contributing again to the trust fund.

So we ought to just take a look at the way Social Security was set up in the beginning, right? We didn't make a distinction with respect to sex, we didn't make a distinction with respect to whether you ended up being a bricklayer or a lawyer. I suppose it is less likely, but maybe the lawyer may make less and the bricklayer may make more.

There is the old story about the plumber who went to fix the lawyer's faucet and after about 15 minutes of work the guy said, "That will be $100," and the lawyer, surprised, exclaimed, "How can you charge $100 for a half hour's work? I only make $35 an hour." The plumber said, "That's all I made when I was a lawyer."

So, I mean, the idea is if we ever start tinkering—and we probably tinker too much with some of these distinctions—I think, Mr. Gashel, you make the point as well. I thought you made it eloquently, and we appreciate your testimony. I am delighted to have in the record so many quotes from letters of people relating their own personal difficulty with the limitation, the penalty. CBO would have us believe there isn't any benefit to lower- and middle-income workers, if you noticed.

Mr. LESSARD. I certainly noticed.

Mr. DAUB. Thank you.

Chairman JACOBS. Mr. Lessard, I might add, I asked Ms. Hardy what we should change the official name of the system to, I asked her what she would start calling it. She said in her testimony it was a retirement and survivors' program.

Mr. LESSARD. I understand.

Chairman JACOBS. One question you posed in your testimony was why shouldn't the rich collect the benefits they paid for.

They did not pay for benefits beyond the retirement test, did they?

Mr. LESSARD. As under current law, no.

Chairman JACOBS. They paid under current law, didn't they?

Mr. LESSARD. Congress has changed the law and made dramatic changes for those who paid benefits.

Chairman JACOBS. I appreciate that. Congress has changed law many times in the midstream, but they paid for what was provided under the law when they paid.

Is that not correct?

Mr. LESSARD. The law is a political contract between representatives and people.

Chairman JACOBS. But they did pay for the benefits which were provided under the law when they paid for them.

Isn't that correct?

Mr. LESSARD. Certainly.

Chairman JACOBS. Thank you.

Mr. DAUB. Mr. Chairman, may I add on that point, that is a point we really need to make clear from the beginning. I have to side with the Chairman on that. We may change the law, but the fact is that actuaries take into account that *x* number of us won't live long enough to collect any benefits, and the actuaries take into account there will be a certain number that live to between 65 and 69 who forfeit a certain amount they would otherwise draw. Otherwise the FICA tax itself would have to be higher and we would be thinking more like a pension instead of like an insurance plan.

So what we are debating really is whether or not to change the policy, but we are certainly not going to change that policy by placing too much weight on the argument that this is sort of a breach of contract, that I didn't know when I got to be 65 I was going to get nailed with a penalty.

You know when you are 18 you have got to register for the draft. You know that. You can't just argue that you didn't know it or society wouldn't have the discipline that it needs to enforce any of its rules.

It is a small point, but I think the Chairman is right on that and it is not as weighty an argument as many other of the arguments are that have been made by each of you in your testimony.

Mr. GASHEL. Mr. Chairman, if I may on this, on the question of the contract, we don't ever reach that question as to whether or not it is a contract. The law is the law. It is very clear that with respect to the population that I represent, Social Security has a major impact on their work activity.

It must be considered by each and every blind individual who decides to work or can get an offer to work or not to work. The level of that person's work activity will have to be considered in light of Social Security benefits that are available under the law.

Our problem is that the benefit availability under the law, given the current restraints on earnings, tends to keep a lot of blind people out of the work force, and that is a consequence that we think Congress, number one, needs to be aware of, and, number two, ought to change in order to get more blind people in the work force. If that means changing the contract, then the contract ought to be changed, or whatever it is called; the law ought to be changed.

Chairman JACOBS. I think the point ought to be made on the record, and was made very eloquently by Commissioner Dorcas Hardy several months back in her newsletter, that as far as getting what is paid for in Social Security, the people who paid for Social Security throughout the 1940's and 1950's and 1960's probably never dreamed how great the benefit would be by the time they retired.

Ms. Hardy has heard figures—I have not heard them challenged—the nuclear family, so-called, where the man worked and the woman worked but did not work under covered employment, worked in the home, that person retiring in 1987, including at the time those born in the so-called notch years, having paid the maximum amount into Social Security for all of his working experience, would receive benefits for himself and his spouse, would receive everything he had paid in plus interest at T-bill rates through those years in about 3½ years. After that it was entirely a subsidy or

transfer payment from one generation to the next, and transferred by people who are now scheduled not to get anything quite so generous when they retire in the next century.

I think it is important for the record to reflect that in terms of what was paid for.

When the tax was put on Social Security benefits, half of Social Security benefits in 1983 as part of the bailout, a consequence of the recession, only one person in my community wrote to tell me he thought it was right, a person who was in that situation. All the rest complained. That was my father. He is not even my constituent, he is in Mr. Burton's district, and he wrote and said it was about time they did something like that. He felt like backing up to take the benefits that he was paid after paying the maximum all of his working years.

So I think a word has to be said for the people, many of whom are paying more in FICA taxes today than they are paying in Federal income taxes, full-time workers. I think that necessarily must be put in balance.

As a servant says in "A Man for All Seasons," I wish rainwater were beer. I don't, but he did. But in the end, we have to deal with some realities and the demands by different groups who ask what their country can do for them, rather than asking not, have to be considered in the equation.

Someone wrote about whether this democracy can be a success or failure, because in a dictatorship you don't have to have self-discipline. Discipline is imposed upon you. I think we need more citizens like my father, who tend to look more objectively to their own pocketbooks and also the well-being of their children and children's children and so on than the rest of society, or this democracy can't work.

If everyone has to have a tax cut and everyone has to have an appropriation, we will take this country by a short route to chaos, I think.

Mr. DAUB. Mr. Chairman, my father wrote me and told me the same thing.

Chairman JACOBS. Very good. No wonder we turned out so well.

Mr. DAUB. Mr. Chairman, before you close the hearing, may I offer for the record a statement by a member of the committee, Mr. Crane, who could not be here, a distinguished Member on my side of the aisle from Illinois.

[The statement follows:]

STATEMENT OF HON. PHIL CRANE

Mr. Chairman, I want to thank you for scheduling this hearing on the retirement earnings test. I expect most of today's witnesses will advocate repeal of the test, because it is an idea whose time has come.

I've been interested in seeing the McDonald's Restaurants recent ads recruiting senior citizens to serve up Big Macs. While on one level the ads depict a growing shortfall in teenage labor that will become steadily more acute, they also underscore the strong desire of many senior Americans to participate in a free enterprise system.

I must admit to some disappointment in the September CBO study which is the focus of this hearing. While CBO was unusually creative in expressing the same findings in a variety of ways, the data are limited to census data from the current population survey. That survey captures self-reported household income, but doesn't measure the impact of the retirement test on specific benefit levels.

Consequently, CBO has presented its findings in an all or nothing approach, that is by categorizing the portion of workers affected by various threshold levels. Yet clearly, those workers who earn under $8,400 in 1988 are affected by that cap not simply those whose earnings exceed it. The cap limits the amount workers may earn before losing benefits. It is only upper income workers who can afford to work in spite of the lost benefits, and that is the picture CBO draws.

Mr. Chairman, there are many good demographic and economic reasons to encourage middle income workers to extend their working lifetime if they are so motivated. But, let me suggest that the surtax for the Medicare Catastrophic Act, just enacted, may be the most compelling reason for taking action, if not in this session, early in the 101st Congress.

Let me thank today's witnesses for taking the time to appear before us today

Chairman JACOBS. For your benefit, Mr. Gashel, you probably always wondered what Mr. Crane looked like, and you don't know what Superman looked like. I can only tell you they look alike.

Mr. DAUB. We have from Congressman Armey for the record before the House Social Security Subcommittee testimony that he would like to have offered along with a series of editorial newspaper clippings from a hearing he held in his subcommittee on this subject.

Chairman JACOBS. I do not object.

Mr. DAUB. And I would offer, Mr. Chairman, a notation of the printouts of the various bills that have been introduced in the House and the Senate in the 100th Congress that relate to the subject of today's hearings.

Chairman JACOBS. Without objection, so ordered.

The hearing is concluded. Thank you for your contributions to the record.

[Whereupon, at 2:35 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

STATEMENT OF CONGRESSMAN ARMEY

FOR RECORD OF THE HOUSE SOCIAL SECURITY SUBCOMMITTEE

HEARING ON THE EARNINGS TEST

SEPTEMBER 29, 1988

THANK YOU FOR INVITING ME TO TESTIFY ON THE SOCIAL SECURITY EARNINGS TEST. THIS IS AN IMPORTANT SUBJECT AND ON DECEMBER 9TH OF LAST YEAR, THE TASK FORCE ON REGULATORY REFORM OF THE REPUBLICAN RESEARCH COMMITTEE, WHICH I CHARI, HELD AN INFORMAL HEARING TO LOOK AT THE SOCIAL SECURITY EARNINGS TEST. REPUBLICANS HAVE LONG DESIRED TO REPEAL WHAT IS ESSENTIALLY A 50% MARGINAL SURTAX ON EARNED INCOME FOR LOW INCOME ELDERLY, AND WE WANTED TO SEE WHAT OUTSIDE GROUPS THOUGHT OF THE IDEA AND HOW THEY WOULD IMPLEMENT THE NEEDED CHANGES. BOTH REP. ARCHER AND REP. DAUB WERE KIND ENOUGH TO ATTEND THE HEARING AND OFFER THEIR THOUGHTS ON THE QUESTION.

WHEN WE DECIDED TO HOLD LAST YEAR'S INFORMAL HEARING, WE UNDERSTOOD THAT A NUMBER OF LEGISLATORS HAD OBJECTIONS TO A STRAIGHT AND TOTAL REPEAL. THUS, WE DECIDED TO HAVE A MULTIPLE CHOICE ON THE EARNINGS TEST QUESTION: SHOULD WE REPEAL, MODIFY OR LEAVE THE EARNINGS TEST AS IS. BECAUSE OPPONENTS HAD RAISED OBJECTIONS ON BOTH FAIRNESS AND BUDGETARY GROUNDS, WE HOPED TO LEAVE GROUND FOR SOME COMPROMISE.

BUT TO OUR SURPRISE, ALL THE GROUPS WE HEARD FROM AGREED THAT SOONER OR LATER THE EARNINGS TEST SHOULD BE TOTALLY ELIMINATED. THIS SURPRISED ME TO SOME EXTENT. I FELT THAT MANY WOULD SUPPORT SOME LIMIT FOR FAIRNESS SAKE OR BUDGETARY REASONS BUT THAT WAS NOT THE CASE. FROM THE NATIONAL COMMITTEEE FOR THE PRESERVATION OF SOCIAL SECURITY TO THE AMERICAN ASSOCIATION OF RETIRED PERSONS TO THE NATIONAL ALLIANCE OF SENIOR CITIZENS, ALL AGREED THAT

ULTIMATE REPEAL OF THE EARNINGS TEST IS VERY DESIRABLE.

I FELT THAT PERHAPS THE VIEWS OF THESE LOBBYING GROUPS REFLECTED A "BELTWAY" MENTALITY NOT FOUND BACK HOME IN OUR DISTRICTS SO I WROTE TO THOSE VOTERS IN MY DISTRICT CONCERNED ABOUT ELDERLY ISSUES AND ASKED HOW THEY FELT ABOUT THE EARNINGS TEST. THE AMOUNT OF MAIL I RECEIVED BACK INDICATED STRONG OPPOSITION TO THE SOCIAL SECURITY EARNINGS TEST.

THE REASONS BOTH THE NATIONAL LOBBYING GROUPS AND VOTERS BACK HOME OPPOSED THE EARNINGS TEST ARE SIMILAR AND YOU ARE ALL PROBABLY AWARE OF THEM. BUT THE TRUE IMPORTANCE LIES IN WHO SUPPORTED TOTAL REPEAL AND WHY. NONE OF THE VOTERS IN MY DISTRICT WHO RESPONDED ARE FAT CATS. IF THEY EARN HUNDREDS OF THOUSANDS, SOCIAL SECURITY FUNDS ARE NO CONCERN. NOR ARE GROUPS LIKE ROOSEVELT'S NCPSSM AND AARP LIKELY TO SUPPORT A BILL THAT IS A WINDFALL TO THE RICH.

INSTEAD, IT WAS LOW WAGE, FULL-TIME OR AVERAGE WAGE PART-TIME ELDERLY WHO FELT BURDENED AND CHEATED BY THE EARNINGS TEST. THE PARELLELS BETWEEN THE NATIONAL LOBBYING GROUPS AND VOTERS IN MY DISTRICT WAS ALMOST PERFECT. LET ME SUMMARIZE SOME OF THE PARTICIPANTS STATEMENTS AND COMPARE THEM TO THOSE OF MY CONSTITUENTS:

-- ROBERT MAXWELL OF AARP SAID THAT LOW TO MODERATE INCOME ELDERLY RELY HEAVILY ON SOCIAL SECURITY BENEFITS. BECAUSE THEY HAVE LIMITED RETIREMENT ASSETS SET ASIDE, THEY NEED TO SUPPLEMENT THEIR INCOME WITH WAGES. AND FROM MY CONSTITUENTS, I GOT LETTERS SAYING "I CANNOT SUPPORT MY FAMILY WITHOUT A SALARY THAT EXCEEDS THE LIMITS FOR SOCIAL SECURITY RECIPIENTS. I AM THEREFORE COMMITTED TO FULL TIME WORK UNTIL THE AGE OF 70...ON THE OTHER

HAND, I HAVE FRIENDS WHO HAVE RETIRED, LIVE IN FLORIDA, HAVE CONSIDERABLE EARNINGS FROM INTEREST AND DIVIDENDS, AND STILL DRAW DOWN 100% OF THEIR SOCIAL SECURITY BENEFITS... WHY IS THIS CHANGE MOVING SO SLOWLY."

ANOTHER MAN WHO EARNED ABOUT $18,000 FIGURED THAT HE COULD QUIT WORKING AND RELY ENTIRELY ON SOCIAL SECURITY BENEFITS AND BE BETTER OFF THAN IF HE WORKED. APPARENTLY, THOUGH, HE HAD SOME PENSION INCOME THAT PUSHED HIS BENEFITS OVER THE $25,000 CAP FOR TAXATION OF BENEFITS. THEREFORE, HIS EFFECTIVE TAX RATE WAS, ACCORDING TO HIS CALCULATIONS, OVER 100%. ANOTHER LADY POINTED OUT HOW HER FAMILY WAS HAVING TO HELP SUPPORT HER BECAUSE HER WORK AND THE EARNINGS TEST BURDEN LEFT HER WITH TOO LITTLE INCOME TO SUPPORT HERSELF. SHE FEELS SHE IS A BURDEN FOR HER FAMILY EVEN THOUGH SHE WORKS.

MARTHA MCSTEEN OF AARP AND FORMER COMMISSIONER OF SOCIAL SECURITY NOTED THAT THE EARNINGS TEST WAS A PAPERWORK BURDEN OF TREMENDOUS PROPORTIONS. AGAIN, THIS CORRESPONDED TO WHAT MY CONSTITUENTS SAY. ONE POOR SELF-EMPLOYED MAN WHO EARNED $10,000 A YEAR SENT ME THE NUMEROUS FORMS AND ESTIMATES THAT ARE NEEDED TO SHOW HOW MUCH WAS EARNED AND WHAT PENALTIES ARE ASSESSED. I CAN SEE WHY 50% OF THE PAYMENT ERRORS BY SOCIAL SECURITY ARE DUE TO THE EARNINGS TEST PAPERWORK. I MIGHT ADD THAT AS A SELF EMPLOYED WORKING ELDERLY PERSON, THIS MAN IS IN AN EFFECTIVE MARGINAL TAX BRACKET OF 80% PLUS. (50% EARNINGS TEST PLUS 15% INCOME TAX PLUS A 15% FICA TAX).

CURT CLINKSCALES OF THE NATIONAL ALLIANCE OF SENIOR CITIZENS ADDED THAT AMERICA IS LOSING A VALUABLE ASSET BY MANDATING RETIREMENT THROUGH THE EARNINGS TEST. ALMOST ALL THE LETTERS I RECIEVED REINFORCED THIS POINT. IN A EARLIER TIME, AMERICA VALUED SELF SUFFICIENCY AND THE WORK ETHIC. ONE MAN WROTE, SAYING " IF A YOUNG MIND IS A TERRIBLE THING TO WASTE, THEN I SUBMIT

THAT A WISE OLD MIND IS A "WONDERFUL THING TO UTILIZE." FURTHER MANY ELDERLY FELT NOT ONLY CHEATED BUT INSULTED. THEY WERE TOLD THAT SOCIAL SECURITY WAS A PENSION AND YOU WOULD GET BACK WHAT YOU PAID IN. THE EARNINGS TEST SAID NO YOU DON'T GET BACK WHAT YOU PAID IN. THIS EARNINGS TEST WAS RATIONALIZED AS A MEANS TEST, AND THUS PRESENTED SOCIAL SECURITY TO THE ELDERLY AS A WELFARE PROGRAM.

I MIGHT ADD THAT THE ADMINISTRATION AND THE COMMISSIONER OF SOCIAL SECURITY HAVE BEEN LOOKING AT WAYS TO REPEAL THE EARNINGS TEST FOR SOME TIME. WHEN THE NEW YORK TIMES REPORTED ON NOVEMBER 29, 1987 THAT THE ADMINISTRATION WAS LOOKING FOR A WAY TO FREE PENSIONERS FROM THE EARNINGS LIMIT, A FLOOD OF EDITORIALS RESPONDED. I'D LIKE TO SUBMIT FOR THE RECORD KEY QUOTES FROM SOME OF THE NUMEROUS EDITORIALS, AS WELL AS THE NEW YORK TIMES ARTICLE ITSELF.

REPEALING THE SOCIAL SECURITY EARINGS TEST:

NEWSPAPERS AND OPINION LEADERS JOIN THE DEBATE

Editorials from Across the Nation
within the time frame of mid-1987 to January, 1988.

"Opponents of repeal argue that there would be substantial short-term cost because benefits would go up for people with those outside earnings. In the real world, however, the opposite would happen. Those cost would be quickly overwhelmed from the additional tax receipts on the extra incomes earned."

-- Forbes Magazine, 12/28/87

"No American should be discouraged from working, as long as he wants to and is physically able to do so. And as the label 'entitlement' implies, he is entitled to the benefits he invested in over so many work years."

-- Cincinnati Enquirer, 12/9/87

"Social Security pensioners over 70 have no earning limit beyond which

they are, in effect, penalized by loss of benefits. Nor does the law apply to income from such sources as private pensions, capital gains, or interest and dividends."

-- Houston Post, 12/7/87

"On the other hand, [Social Security Subcommittee Chairman,] Rep. Andy Jacobs Jr., D-Ind., argues that repealing the limits would be a windfall for the wealthy. He said that 'lawyers who are 66 years old and are capable of making a salary of $100,000 will still be able to collect full Social Security benefits.'

"Jacobs, however, ignores the fact that a non-working 66-year-old can collect $100,000 in interest and dividends without losing Social Security benefits. Nor apparently does Jacobs have any problem with denying Social Security to that 66-year-old attorney but not to his 70-year-old partner."

-- Indianapolis Star, 12/6/87

"Imagine you are 66 years old, a widow, living on $6,000 in Social Security benefits and some money you earn in a part-time job. Imagine further that you have the opportunity to convert your part-time job to full-time and you could be making $11,000 a year.

"Sounds great, until you remember that under present Social Security rules a pensioner cannot earn more than $8,160 a year without having to give up part of the Social Security benefits. You would lose some $1,400 in Social Security benefits and would at the same time have to pay Social Security and income taxes on your earnings. A quick calculation shows that a full-time job does not leave you with much extra income over the part-time one. So why work full-time?"

-- The Wilmington News Journal, 12/5/87

"The people most hurt by the Social Security earnings limit are those who most need some extra earnings.

What's wrong with the limit? For starters, it's an EARNINGS limit, not an INCOME limit. Those who have huge incomes from pensions or investments don't lose a dime in Social Security benefits. Those who earn more than $8,160 a year bagging groceries do.

"In other words, the limit is a work tax, pure and simple.... Who can justify a 50 percent tax on some of the neediest Americans, while the Tax Reform Act of 1986 guarantees a top rate of 28 percent for the wealthy?"

-- Rochester Democrat & Chronicle, 12/4/87

"Setting politics aside, there is much to be said for Dr. Bowen's suggestion. Unfortunately, there also is much to be said against it, starting with its cost: about $7.5 billion over five years."

-- Pittsburgh Post, 12/4/87

"There is a further argument that Bowen didn't make: Because Social Security operates through a trust fund supported by an earmarked payroll tax, depending on revenue that cannot legally be used for any other purpose,

it should not be counted as part of the general federal budget."

-- Eugene Register Guard, 12/4/87

"The Secretary's view is realistic. For medical and nutritional reasons, Americans 65 through 69 do not feel as tired as their counterparts did a generation or two ago. Consequently, many want to keep on working. But disillusioned by that infernal Social Security retirement test, they are tempted to circumvent the restriction by not reporting some income.

"Hence, the 'underground economy' gets the action while the federal Treasury is shorted. The message is clear: When otherwise law-abiding people are tempted to underreport income, it is time to examine the cause. If a law is to blame, then Congress had better consider changing the law."

-- Cedar Rapids Gazette, 12/3/87

"If doing away with the cap is unpalatable, perhaps a formula could be worked out for a sliding scale: for example, no reduction in benefits until $10,000 is earned, then a $1 reduction for every $4 earned up to $20,000, $1 for every $3 earned up to $30,000, and so on. Benefits could then be a supplement for income instead of a substitute. Those who have paid into the Social Security trust fund for so long should not have to sharply curtail their income to receive the benefits they are due."

-- St. Louis Post-Dispatch, 12/3/87

"But the proposal's immediate financial effect could be minimized if the earnings restriction were discarded gradually rather than all at once. Why not phase out the limit over five years, abolishing it for the 69-year-olds one year, 68-year-olds the following year and so on?"

-- Dallas Mornings News, 12//87

"The earnings cap is an outmoded concept that hark[en]s back to Depression-era thinking. It is also regressive -- penalizing low-income retirees for working while ensuring a tax-sheltered bonus for those who can afford to withdraw from the labor market at 65."

-- St. Petersburg Times, 12/3/87

"It also can be argued that the rule discriminates most against one of the groups Social Security was intended to help: wage earners for whom Social Security is an important pillar of support.... For the working stiff who needs both benefits and wages to get by, or who simply enjoy working and have something to contribute to society, the penalty kicks in at a ridiculously low earnings level, $8,160, after which $1 of benefits is lost for every additional $3 earned."

-- San Jose Mercury News, 12/2/87

"So the oldster who sits at home and does nothing is treated by the law with more sympathy than he or she with a lot of energy to contribute... To tell them they cannot work when they want to is to repudiate many of the virtues that they spent a life time teaching us."

-- South Bend Tribune, 12/2/87

"The government's strange attitude shows once again why Social Security itself should be converted into a private system. No private retirement system would ever discourage its recipients from working at other jobs. Retirement benefits are too important to be left to a government that understands little about the retirees it claims to serve."

-- The Orange County Register, 12/1/87

"The time has come to erect safeguards to protect the financial independence of Social Security.

"There are, however, substantial reforms that can be made without undermining the fiscal integrity of the program and we favor a number of them....

"Dr. Otis R. Bowen, secretary of Health and Human Services, has already proposed one of these: lifting the limit on work earnings that now discourages persons eligible for Social Security from staying on the job...

"Another promising reform would increase the incentives for postponing Social Security. Under existing laws, benefits are increased by 3% for each year retirement is postponed through the 69th birthday. That is a paltry return. But if the return were increased to 8%, according to a study by the House Republican Research Committee, it would achieve actuarial fairness and encourage broader participation."

-- Los Angeles Times, 12/3/87

"We think it is time that the law, not the older workers, be retired."

-- The San Diego Tribune, 12/2/87

"A cap on earnings for Social Security recipients is fair. The program is intended to help replace earnings for those no longer working.

"Lifting the cap would most help those who least need assistance. A better chance would be to tie Social Security benefits more closely to need by imposing higher taxes on benefits for those with substantial other income."

-- Salinas Journal, Kansas, 12/6/87

"The compromise [on Social Security in 1983] resulted in a series of tax increases for wage-earners and employers to keep the Social Security Trust Fund adequately funded... Up to half the benefits for retired persons who have high unearned income (and earned income for the 70-year-olds) is taxed now. Congress should consider additional means testing to ensure that those who need benefits the most get them.

The 70-and-over provisions should be repealed. It is not right for persons who make high salaries, or who pay themselves high salaries, to get full Social Security benefits just because they are healthy

septuagenarians.... It [Social Security] should remain as a safety net for the elderly, low-income widows and their children and the disabled. Making it a pension for the well-to-do will erode the trust fund."

-- Hamilton Journal News, 12/6/87

"What a strange time for Otis Bowen, Secretary of Health and Human Services, to float his new Social Security balloon. Just days ago, Congressional and White House negotiators gave up trying to cap automatic cost-of-living increases in Social Security benefits....

"Yet now, Dr. Bowen dares to propose LIBERALIZING Social Security benefits by dropping the limits on payments to those who work past age 65... Still, it is not wrong to encourage willing older adults to remain in the work force. The idea makes sense, however, only in the context of reforms in Social Security as a whole...

"Today, however, the rule is highly criticized as unfair and inefficient. It's unfair because there is no such reduction for so-called unearned income from investments...

"One remedy would be to treat investments income like earned income in the calculation of benefits. But that would encourage further dependence on Government, reducing incentives for younger workers to save for retirement. Then why not simply dump the earned-income test?

"That's [the cost of repeal] not the only way to put $7 billion to fruitful use. And it is a particularly unseemly way to spend Federal resources given the budget negotiators' cowardly failure to ask middle-income retirees to give up a penny in Social Security increases... Too bad, because it could be part of an intelligent program to rationalize the incredibly valuable -- and incredibly expensive -- Social Security program."

-- New York Times, 12/6/87

"America's elderly enjoy a persuasive voice in Washington since they account for roughly 12 percent of the electorate and have a formidable lobbying program. It is estimated that the government spends $6 on benefits for the age 60-plus population to every $1 it spends on benefits for children.

"Bowen's plan would exacerbate such benefit inequities and erode the further relationship between generations. Pursuing the politics of ageism, which pits one age group against another, generates resentment and sullies the national idea of improving the quality of life for all citizens."

-- Atlanta Journal, 12/4/87

"[Social Security Commissioner Dorcas] Hardy says the current law 'has driven a large underground economy.' In order to keep collecting full Social Security benefits, she explains, many recipients simply neglect to tell the government about thejr earnings. If that is true, why doesn't she put the emphasis on prosecuting violators rather than on eliminating the temptation to cheat?

"Of course, it may be that the $8,160 limit on earnings needs to be raised somewhat, but that's not the argument that Bowen and Hardy are making."

-- Milwaukee Journal, 12/3/87

"Social Security was designed as an income replacement, not a supplement, so it makes sense to defer some benefits for those with significant outside earnings. And by encouraging older workers to accept guaranteed retirement compensation in lieu of continued work, Social Security creates new opportunities for the young."

-- Los Angeles Herald, 12/2/87

"The Social Security benefit structure is a delicate mix of what a beneficiary has paid in and what he needs. Repeal of the earnings test would alter both this mix and, as proponents well understand, the principles on which the system is founded. The change would not be healthy. Should the earnings test be eased a little to help retirees of modest means? Is that one of the early things to be done as the deficit comes down and a few funds become available? We don't know. But certainly there can be no justification for repeal."

-- Washington Post, 12/2/87

"Setting politics aside, there is much to be said for Bowen's suggestion. Unfortunately, there is also much to be said against it, starting with its cost: about $7.5 billion over five years."

-- Evansville Courier, 12/7/87

SO IN SUMMARY, I THINK THE CASE FOR REPEAL -- MAYBE NOT IMMEDIATELY BUT SOON -- IS JUSTIFIED BECAUSE IT IS NEEDED FOR ELDERLY WORKERS TO SUPPORT THEMSELVES. TOTAL REPEAL WOULD CERTAINLY BENEFIT UPPER INCOMES WHO HAVE CONTINUED TO WORK DESPITE THE EARNINGS TEST. BUT, THE REAL WINNERS WOULD BE THOSE LOWER AND AVERAGE INCOME ELDERLY WHO HAVE BEEN FORCED TO QUIT WORK BECAUSE OF THE EARNINGS TEST. THE EARNINGS TEST AMOUNTS TO MANDATORY RETIREMENT, THE STRONGEST REMAINING BURDEN ON ELDERLY WORKERS. BUT ITS EFFECT IS TARGETTED TOWARDS THE LOWER INCOME -- FULL TIME ELDERLY EARNING AROUND THE MINIMUM WAGE. IN FACT, IF WE RAISED THE MINIMUM WAGE TO THE ULTIMATE LEVEL RIGHT NOW, ALL ELDERLY WORKING FULL-TIME AT MINIMUM WAGE WOULD BE IN AN EFFECTIVE 72% MARGINAL TAX BRACKET. THAT IS NOT THE AVERAGE WAGE BUT AT THE MINIMUM WAGE. WHY WE RESERVE THIS BURDEN ONLY FOR THE ELDERLY IS INDEFENSIBLE, AND I HOPE THIS COMMITTEE ACTS TO CHANGE THE EARNINGS TEST AS SOON AS POSSIBLE.

"All the News That's Fit to Print"

The New York

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REAGAN GETS PLEA TO FREE PENSIONERS OF EARNINGS LIMIT

BOWEN PLAN UNDER STUDY

Secretary Says Social Security Law Puts an Unreasonable Tax on Elderly's Wages

By ROBERT PEAR
Special to The New York Times

WASHINGTON, Nov. 28 — Top officials at the Department of Health and Human Services are urging President Reagan to seek repeal of a law that reduces Social Security benefits for elderly people who earn more than $8,160 a year.

Dr. Otis R. Bowen, the Secretary of Health and Human Services, and Dorcas R. Hardy, the Commissioner of Social Security, both say the law punishes people for working and forces many to retire for economic reasons although they would prefer to work.

'Unreasonable 50 Percent Tax'

In a confidential memorandum to Mr. Reagan, Dr. Bowen said the law "imposes an unreasonable 50 percent tax on the earnings of the elderly" and "discourages productive labor."

Social Security officials said the limit on earnings was one of the most unpopular features of the program. In an interview, Miss Hardy said she believed some Social Security beneficiaries tried to circumvent the restriction by not reporting income to the Government. She said that in this way the current law "has driven a large underground economy."

'Good Policy and Politics'

In his memorandum, Dr. Bowen said the proposal to repeal the earnings limit was "both good policy and good politics" because it would be "popular among elderly voters," would "eliminate a major work disincentive" and would help the economy by keeping millions of skilled workers in the labor force.

Dr. Bowen acknowledged that his proposal could theoretically have "substantial short-term costs," perhaps

Continued on Page 44, Column 1

8 Latin Chiefs Urge Cuba Role In Their Region

Meeting Without U.S., Leaders Stress Unity

By LARRY ROHTER
Special to The New York Times

ACAPULCO, Mexico, Nov. 28 — The presidents of eight Latin American countries, meeting here for their first summit conference held without the participation of the United States, agreed today that Cuba should be invited to rejoin regional organizations from which it was expelled more than two decades ago.

"There is a consensus among the presidents that we ought to struggle for the total integration of Cuba into the inter-American system," President José Sarney of Brazil said this morning. Mr. Sarney also said that Cuba's presence in such regional organizations was "indispensible" to their normal functioning.

The initiative on Cuba was the first major surprise of the four-day conference, called to discuss regional problems such as the conflict in Central America and Latin America's foreign debt of nearly $400 billion. Argentina, Brazil, Colombia, Panama, Peru, Uruguay and Venezuela are participating in the conference, in addition to the host country, Mexico.

Consistent Opposition From U.S.

Cuba was expelled from the Organization of American States in the 1960's following pressure by the United States on the Latin American and Caribbean members of the group. It is also not a member of the hemisphere's two major economic groups, the Inter-American Development Bank and the Latin American Association for Development and Integration.

The United States has consistently opposed Cuban participation in regional organizations and led efforts to isolate Cuba diplomatically. It argues that Cuba should properly be considered a member of the Soviet bloc and should not be readmitted to hemispheric groups until it installs democratic institutions, improves its human rights record and agrees not to interfere in the affairs of its neighbors.

Until recently, Mexico was the only Latin American country to maintain

Continued on Page 34, Column 3

Nuns at election headquarters in Port-au-Prince, Haiti, sort

Moscow Is Seen at Turning P In Its Intervention in Afgha

By JOHN KIFNER
Special to The New York Times

KABUL, Afghanistan, Nov. 28 — The Soviet Union's eight-year intervention in Afghanistan is at a crucial moment, Western diplomats here and in Moscow say, with Moscow increasingly desperate to find a way to pull out its 115,000 troops at a time when the Afghan regime is losing ground to the Islamic rebels.

Afghanistan is expected to be a major topic at the coming summit conference between the Soviet leader, Mikhail S. Gorbachev, and President Reagan, with reports circulating in diplomatic circles that the Soviet Union may offer a timetable for a 12-month withdrawal in exchange for a halt in American aid to the rebels.

'Bleeding Wound'

Mr. Gorbachev has called his country's involvement in Afghanistan a "bleeding wound." Soviet troops moved into the country at the end of 1979 to stop infighting among the local Communists and, they asserted, to protect [illegible] by Islamic rebels [illegible]

But the dilemma for Moscow, Western diplomats in the two capitals agree, is that the withdrawal of Soviet troops would now almost inevitably mean the collapse of the Government headed by Lieut. Gen. Najibullah.

"This is the beginning of the end," a Western diplomat here said flatly. "Without Soviet troops, I am convinced

"There's a real sense an end-game," said one in this dusty capital, w women washing vegetal sparse pools of Kabul R the center of town, wh Soviet helicopters skirt j ing mountains, throwing heat flares to ward off missiles.

The Stinger anti-airc supplied by the United St Islamic rebel groups, colle as the mujahedin, or l have drastically changed the war in the past year, military experts here say.

Guerrillas were down Afghan aircraft with Sti of better than one a day according to intelligence summer. This level of has forced the Soviet Uni the helicopter gunship re hit-and-best tactic against the crusade, the vast count rebels and to concentrat in defending Kabul and major cities.

"A year ago, rebel mar here, they were crying said a Western diplomat as the purely military e chological effect on the confidence is enormous."

Coinciding with the about is a growing sens

2 Big West Side Projects Fuel Anti-Development Sentiment

By JANE GROSS

Two gigantic building projects proposed for the West Side of Manhattan have prompted a groundswell of opposition so broad and deep that a number of urban experts and politicians say it has changed the way New Yorkers look

[illegible] vyn Kaufman, who, with a $25,000 donation, is the largest individual contributor to the Municipal Art Society's legal effort to block the Coliseum project.

"Don't ever sell the public short," Mr. Kaufman said. "You irritate them [illegible] long enough and they'll rise up and

has been Mr. Lusc, who according to the polls is running second in the Re-

BOWEN WOULD END LIMIT ON EARNINGS

Continued From Page 1

$7.5 billion over five years, because Social Security benefits would rise for some people with outside earnings. But in the long run, he said it would "contribute to the reduction of the Federal deficit" because elderly people would work more, generating additional income taxes and payroll taxes.

White House officials said they were studying the proposal. John K. Meagher, an Assistant Secretary of the Treasury, said his department "generally supports the concept of repeal as a matter of good economic policy," but he expressed concern about "the short-term budget effects."

One of the main reasons for the earnings test is that Social Security was intended to replace a portion of the earnings lost as a result of retirement, disability or death. A person who continued working beyond the normal retirement age was presumed to have less need for the full benefit.

Under current law, a person's Social Security benefits are reduced by $1 for every $2 of earnings above $8,160 for people 65 to 69 years old. The limit on such retirement earnings does not apply to people 70 or older.

A 65-year-old person who receives a typical Social Security benefit of $6,000 a year begins losing benefits after he has earned $8,160 in wages. The person loses the entire benefit if he earns $20,160 or more.

But there are no such limits when the income is from a pension, interest, dividends or capital gains achieved through the sale of stock or other assets. Dr. Bowen said the difference in treatment of earned and unearned income was unfair.

'Issues Hurt Republican Party'

In addition, his memorandum says, "Social Security issues have hurt the Republican Party badly in this decade." A Presidential proposal to eliminate the earnings limit would permit Republicans to seize the offensive on an important issue while "stressing such Republican themes as the need for tax rate reduction, the dignity of labor and the folly of Federal intrusion into the realm of private decisions," Dr. Bowen said.

The proposal has extraordinarily broad support among members of Congress, ranging from liberal Democrats, like Representative Barney Frank of Massachusetts, to conservative Republicans, including Representatives Bill Archer and Dick Armey of Texas and Jack F. Kemp of upstate New York.

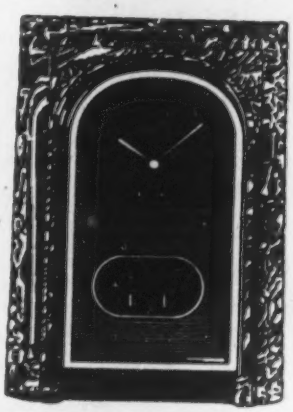
Gradual Process Acceptable

Dr. Bowen hinted that he would be willing to accept cutbacks elsewhere in his department if necessary to offset the cost of his Social Security proposal. He said he would prefer to see the earnings limit abolished immediately. But to minimize the cost, he said, it could be discarded gradually over several years, starting with workers 67 to 69 years old.

Dr. Bowen said, "The cost of this proposal is quite small when considered in the context of the entire Social Security program," which paid more than $260 billion in benefits last year. He noted that the Social Security trust fund was expected to run surpluses for several decades under current law.

The President's Council of Economic Advisers, in a report on the economic status of the elderly, said, "Even if the earnings test does reduce budget outlays, it is still hard to defend" because it "reduces the contribution of the elderly to the total output of the economy."

Seiko



TIME ON ICE

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Lobby

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STATEMENT OF REP. HANK BROWN
ON THE SOCIAL SECURITY RETIREMENT TEST
BEFORE THE SUBCOMMITTEE ON SOCIAL SECURITY
COMMITTEE ON WAYS AND MEANS

SEPTEMBER 29, 1988

Mr. Chairman, as a cosponsor of a bill (H.R. 1204) to repeal the Social Security retirement test, I appreciate the opportunity to appear before the committee today.

With all the talk about the need for economic competitiveness and greater productivity, the United States has made a major blunder by penalizing Social Security recipients age 65 to 69 who wish to work.

This is why I have introduced H.R. 1204 to repeal the Social Security retirement test which is aimed at our senior citizens who desire to be productive. The penalty is unfair to those who have contributed to Social Security and damages our economy. Rather than penalizing people for working, we should reward those who wish to work.

This "earnings penalty" now requires that Social Security benefits be reduced $1 for every $2 earned in excess of an annual exempt amount. The annual amount in 1988 is $8,400 for persons age 65 to 69 and $6,120 for persons under age 65.

For example, if you are age 67 and earn, say, $8,700 this year, you will earn $300 more than the exempt amount, and your Social Security benefits will be reduced by one-half of the excess or $150. The penalty is not applied to persons age 70 or older.

Problems Created

Two problems are created by the earnings penalty. First, it is difficult for some to maintain their pre-retirement lifestyles without working. They are caught in a cruel trap because by working they will lose part of their benefits if they earn more than the annual exempt amount.

Second, our population is getting older. And as the population ages, the relative size of the work force grows smaller. With a relatively smaller work force, it will be more difficult for the U.S. economy to support those drawing retirement benefits.

Today, approximately 11.7 percent of the U.S. population is age 65 and older. In the next century, over 21 percent, or one-fifth, of the population will be of retirement age, according to the actuarial figures in the 1988 Annual Report of the Board of Trustees of the Social Security Trust Funds.

Benefits

Removing the earnings penalty for those over age 65 would allow those able to and interested in working to continue to do so without the fear of losing Social Security benefits. They could strive to maintain their pre-retirement lifestyles, without the current catch-22 to hold them back.

Leaving open the option to work will not only benefit our senior citizens, but the entire nation as well. Repealing the earnings penalty will open up an additional source of labor, as our work force grows smaller in relation to the overall size of our population.

This new labor supply will strengthen our economy, by providing needed workers. It also will ease some of the burden of the younger workers whose current contributions to the Social Security program help pay for the Social Security benefits received by our senior citizens. Those senior citizens who work will continue to pay F.I.C.A. taxes on their wages, the same way they do today.

Just as important as the economic benefits is the effect this proposal will have on the morale of our senior citizens. Many people derive a good deal of satisfaction from their jobs. Repealing the earnings penalty will help them retain this feeling of being productive.

It also will show seniors 65 and older that the nation still needs and cares about them, boosting their sense of self-worth. As a result, they are likely to be much happier and healthier individuals, with the positive byproduct of lower medical costs for this population group as a whole.

Associated Costs

With the elimination of the retirement test, the Social Security program would pay out from $4 billion to $5 billion in additional benefits each year. However, these payments will be offset by both the F.I.C.A. and income taxes paid on the wages of those senior citizens who work.

In addition, more senior citizens will have adjusted gross incomes in excess of $25,000 ($32,000 for married couples who file a joint tax return), and thus will pay income taxes on one-half of their Social Security benefits.

According to the Social Security Trustee's report, the Social Security Trust Funds are in good shape and expected to remain that way into the next century. Ending the retirement test would improve those projections by increasing the ratio of workers to beneficiaries.

Some critics may complain that this proposal will add to the federal budget deficit. They are overlooking the major pickup in taxes generated by the new earnings. The truth is that an increase in productive work will improve our economy, increase our competitiveness, and stimulate federal revenue.

Historically, Americans have always been industrious. This attitude has made us a strong nation. We should be proud of this heritage and seek to preserve it. Repealing the retirement test would do just that by encouraging rather than discouraging our senior citizens who are both able and desire to contribute to society.

STATEMENT OF THE HONORABLE BILL CHAPPELL

ON THE SOCIAL SECURITY EARNINGS LIMIT

BEFORE THE SOCIAL SECURITY SUBCOMMITTEE

SEPTEMBER 29, 1988

MR. CHAIRMAN, I APPRECIATE THE OPPORTUNITY TO TESTIFY TODAY ON THE ISSUE OF THE SOCIAL SECURITY OUTSIDE EARNINGS LIMIT.

I HAVE LONG FELT THAT THE OUTSIDE EARNINGS LIMIT DISCRIMINATES AGAINST THOSE ELDERLY WHO WISH TO REMAIN PRODUCTIVE MEMBERS OF SOCIETY BY DEPRIVING THEM OF THEIR LEGITIMATELY EARNED BENEFITS. IN FACT, THE CURRENT LAW CREATES A DISINCENTIVE FOR SENIOR CITIZENS TO RAISE THEIR STANDARD OF LIVING AND PROVIDE FOR THEMSELVES. AFTER ALL, SOCIAL SECURITY WAS NEVER INTENDED TO BE THE SOLE SOURCE OF INCOME FOR RETIREES, BUT THE EARNINGS RESTRICTION OFTEN LEADS TO THAT RESULT.

THE ADMINISTRATION ALSO OPPOSES THE EARNINGS TEST, AS DOES THE AMERICAN ASSOCIATION OF RETIRED PERSONS AND THE NATIONAL COMMITTEE TO PRESERVE SOCIAL SECURITY AND MEDICARE. EVERY MEMBER OF CONGRESS HAS HEARD FROM A NUMBER OF CONSTITUENTS WHO ARE ADVERSELY AFFECTED BY THIS UNFAIR LIMITATION. AT THIS POINT, I WOULD ALSO LIKE TO INCLUDE IN THE RECORD AN ARTICLE BY ECONOMIST ROY E. CORDATO. THIS ARTICLE IS ENTITLED "THE SOCIAL SECURITY EARNINGS TEST: BAD POLICY THEN, BAD POLICY NOW." MR. CHAIRMAN, THERE IS CLEARLY STRONG SUPPORT FOR ITS REPEAL.

I HAVE INTRODUCED H.R. 770, A BILL TO ELIMINATE THE OUTSIDE EARNINGS RESTRICTION. A NUMBER OF OTHER MEMBERS HAVE SPONSORED SIMILAR LEGISLATION. WHILE I REALIZE THERE IS LITTLE TIME LEFT IN THIS CONGRESS FOR PASSAGE OF SUCH A MEASURE, I BELIEVE THE HOUSE WOULD SWIFTLY APPROVE REPEAL LEGISLATION IF GIVEN THE OPPORTUNITY.

ACCORDINGLY, I WOULD URGE YOUR COMMITTEE TAKE ACTION ON EITHER MY BILL OR WHATEVER MEASURE YOU FEEL WILL BEST ACHIEVE THE GOAL OF REMOVING THIS UNFAIR AND UNWISE RESTRICTION ON OUR SENIOR CITIZENS.

I THANK THE CHAIRMAN AND THE COMMITTEE FOR PERMITTING ME TO SHARE MY THOUGHTS ON THIS ISSUE AND I LOOK FORWARD TO WORKING WITH YOU ON THIS AND OTHER PROPOSALS TO IMPROVE OUR SOCIAL SECURITY SYSTEM.

IRET Op Ed

December 21, 1987
No. 57

The Social Security Earnings Test: Bad Policy Then, Bad Policy Now

Since its inception in 1935 the Social Security system has imposed some form of earnings test on those citizens who were otherwise eligible to receive Social Security benefits. Under current law, those retirees who are between the ages of 65 and 70 can earn $8,160 before they start seeing reductions in their social security check while for those under 65 the benefit cut back begins at earnings of $6,000. These limits only apply to wages; retirees are not penalized for earning investment or dividend income. This policy limits both the well being of the elderly and the prosperity of the economy as a whole. Several bills before the Congress would repeal this earnings test, either all at once or through a phasing out process. These efforts should be applauded.

One of the main arguments advanced for the individual income tax rate cuts in the Tax Reform Act of 1986 (TRA 86) is that a lower income tax rate will increase work effort and therefore economic growth. This argument should apply as well in the case of social security but the earnings test disregards it. When the earnings limits kick in, most senior citizens find themselves facing marginal tax rates of over 70%. That is, the combined effect of reductions in social security payments, regular income tax, and other payroll taxes results in most senior citizens being able to keep only 30 cents, or less in many cases, of every additional wage dollar earned. This puts older citizens that are affected by the income limits in a higher tax bracket than any other wage earners. Instead of encouraging older Americans to continue to be as productive as they can be, this burdensome level of taxation sends the opposite message. Within a broad income range, the earnings test says to senior citizens that the more productive they are, and therefore the higher the wages they can command in the market place, the less they should try to be productive. This is both bad economic policy and bad social policy.

Over the years several arguments have been put forth in support of this social security take-back. But these arguments do not justify the policy in terms of promoting either the particular interests of the elderly or the general interests of society. Originally the earnings test was openly supported as a way of pushing the elderly out of the work force in order to "make room" for younger workers. Some persons, including many of those who support repeal, believe that this argument was valid during the great depression, when job opportunities were scarce, but is not valid today. They are only half right; this argument was never analytically sound. It views the economy as static, with a fixed number of employment opportunities. The assumption is that if the number of workers seeking employment is less than the number of jobs available then its all right to encourage older folks to work. But if there is an unemployment problem, as there was during the thirties, then any job an older person gets he must be taking away from a (more deserving?) younger worker.

This argument contains many fallacies, too many to consider here. But the most important might be its fundamental misunderstanding of the relationship between real economic growth and employment. The backbone of a growing economy is work effort, combined with other factors of production, that is accurately directed toward the satisfaction of consumer demands. The more this work effort is encouraged (among members of any age group) the more the economy will grow and the more jobs will be created for everyone; young and old. If anything, the social security earnings test helped to prolong the depression by discouraging productive work effort on the part of older citizens. The only cure for a depression is economic growth. Unfortunately, policy makers during the thirties never learned this lesson.

The modern day justification for continuation of the earnings test is (surprise! surprise!) the budget deficit. Repeal of the earnings test will mean more money paid out in social security benefits, hence a bigger gap between the government's outlays and income. This would be, at most, a short term effect. With more people working, more taxes will be paid (both income taxes and FICA taxes), which would supply additional revenues that could easily offset those lost through additional Social Security payments.

Even if this weren't the case repeal of the earnings test should still be supported. The budget balancing argument misses the point. It as if its advocates believe that a balanced budget has some intrinsic elegance that makes it supportable for its own sake. Supposedly, in balancing the budget the economy will be put on a more sound footing and economic growth will be fostered. Opposing abolition of the Social Security earnings test is tantamount to cutting off your nose to spite your face. This is one of many

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examples where, in attempting to balance the budget, legislators are offering policies that will ultimately retard growth and therefore reduce economic welfare. Balancing the budget will be a positive step for the economy so long as the cures proposed are not worse than the illness. Discouraging work effort and productivity in the name of fiscal responsibility is clearly the wrong road to take. The Social Security earnings test is not now, and never was, a good idea. By discouraging real saving and draining productive resources out of the private economy the Social Security system, as it currently exists, is proving to be an albatross around the economy's neck. The earnings test adds to this by penalizing the productive activities of some citizens simply because of their age. In addition to being bad economic policy the original effect of the test was to discriminate against the elderly. This part of the program has been a success, but clearly not something we should be proud of. Legislative proposals to eliminate the test should be taken up promptly and passed. The sooner this relic is eliminated the better.

Roy E. Cordato
Economist

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P.O. DRAWER 431

ALEXANDRIA, LOUISIANA 71309-0431

4 September 1988

The Ways & Means Committee
U.S. Congress
Washington, D.C.

Gentlemen:

I would appreciate this letter being considered, when your committee holds hearings on the bill to eliminate the earnings requirement for payment of social security pensions.

I have paid the maximum self-employment taxes and social security taxes through my corporation, for some thirty years. Last year, these taxes totaled $6,263.40 for myself and my corporation. I do not consider social security pensions as welfare, since my pension would be much greater if I had entered any annuity program, and made comparable payments.

If it would assist the government, I could understand the restriction on earnings, even though I wouldn't agree with them. After all, there are no similar restrictions on any other pension plans including members of Congress and government employees. But forcing me to take full retirement has little or no benefit to the government! I'd like to begin retirement by slowing down and taking longer vacations. But your rules make it mandatory that I quit or work for nothing. Why you want to force me to cease productive activity just isn't comprehensible.

When you pass the maximum allowable earnings, you lose one-half of your social security benefits. That's a 50% tax any way that you wish to describe it. Self-employment tax is 13.02%. If you happen to own your own corporation, the total social security taxes are 15.02%. That doesn't include unemployment taxes and it's most unlikely that I'll ever receive benefits from that fund. If a person has accumulated any savings over a lifetime, the tax bracket on the additional salary can easily be 33%. State income taxes on the increased income can easily be in a 4% bracket. Add it up and at best it comes to 100%.

I do like to work, but how many people want to work for nothing? I've spent much of my life with voluntary organizations but really hadn't anticipated turning my office into another non-profit affair. With the increase in medicare based on income taxes, it could actually cost my wife and myself $1,600 (and it progressively increases) per year to work!!

I realize that I'll be allowed to earn all I wish when I'm 70, but I have no assurance of reaching that goal. And if I quit now, I'd be worthless in my profession at 70. I want to slow down and quit the 70 and 80 hour weeks. But current legislation makes it all or nothing. It isn't fair and is very bad legislation when it benefits no one and hurts many. Too many productive citizens have been forced to vegitate because of this unique restriction. It's just a portion of my money that I'd like returned.

Sincerely,

Charles F. Buckley, E.A.

Enrolled to practice before the Internal Revenue Service

Charles F. Buckley, president – Edward H. Blackwood, vice president – Terry J. Ducote, secretary/treasurer

STATEMENT BY ROBERT J. MYERS PRESENTED TO THE SUBCOMMITTEE ON SOCIAL SECURITY OF THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, SEPTEMBER 29, 1988, WITH REGARD TO RETIREMENT TEST.

Mr. Chairman and Members of the Subcommittee: My name is Robert J. Myers. I served in various actuarial capacities with the Social Security Administration and its predecessor agencies during 1934-70, being Chief Actuary for the last 23 of those years. In 1981-82, I was Deputy Commissioner of Social Security, and in 1982-83, I was Executive Director of the National Commission on Social Security Reform.

The retirement earnings test under the Old-Age, Survivors, and Disability Insurance program has, over the years, attempted to draw a line between being retired and being employed. In the original Act, this provision was on an "all or none" basis, in that benefits were to be withheld for persons who engaged in "regular employment" (not defined in the law). This concept was changed somewhat in the 1939 Act, before monthly benefits first became payable, so as to establish covered wages of $15 per month as the point at which the person was not considered retired, and therefore no benefits were payable.

Over the years, the earnings test has been changed so as to phase in more smoothly and equitably for persons who have moderate earnings. At present, there is an annual exempt amount -- currently, $8,400 for persons aged 65 - 69 and $6,120 for younger persons -- such that persons with earnings equal to or less than this receive full benefits, whereas those with higher earnings have their benefits reduced by $1 for every $2 of excess earnings, which will become on a $1-for-$3 basis in 1990 for persons at and above the Normal Retirement Age (currently, 65).

Originally, the earnings test applied at all ages. The 1950 Act provided that it should not be applicable after attainment of age 75. Such limiting age was reduced to 72, effective for 1955, and then to 70, effective for 1983. In all logic, there is no reason to have a limiting age beyond which the test does not apply. This basis was adopted solely because of political pressures arising from individuals who argued that, otherwise, they would never get any return on their contributions because they would work all their lifetime.

Individuals who have benefits withheld because of excess earnings are compensated therefor, as to OASDI benefits, through two means. First, the additional earnings result in a recomputation that may increase subsequent benefit amounts -- but this will not always occur, depending upon the current level of earnings as contrasted with that in previous years. Second, future benefits are increased by the Delayed Retirement Credit (DRC), which is at the rate of 3% per year for those who attain age 65 in 1982-89 (1% for those attaining age 65 earlier), but will increase gradually for persons reaching age 65 later. In the long run, the DRC will be at the rate of 8% per year -- for those attaining the Normal Retirement Age in 2009 (when it will be age 66) and thereafter.

It is important to note that, when the DRC is 8%, it will then be approximately the actuarial equivalent. By this is meant that, insofar as the OASDI program is concerned, the long-range cost effect of persons delaying retirement and then receiving larger benefits due to the DRCs will be approximately the same as though benefits were payable automatically at the Normal Retirement Age, regardless of subsequent earnings. It may also be noted that this actuarial equivalency is present for those who now retire before the Normal Retirement Age. Specifically, at present, if an individual retires at age 62, the benefit is 80% of that available at age 65. Thus, if retirement were deferred for 3 years, the benefit would be 25% higher relatively, or about 8% per year of delay.

Over the years, the earnings test has been perhaps the most controversial feature of the OASDI program insofar as the general public was concerned. Many people view it as being unfair because they believe it to be a significant deterrent to continued employment -- which, as I will discuss later, is frequently actually the case. Still other persons believe the earnings test to be unfair because they believe that "they have bought and paid for the benfits to be payable at age 65" -- but this is not a correct conclusion, because the "insurance" provided was against retirement, not against attainment of age 65.

In defense of the earnings test, the basic argument is that it is not appropriate to pay retirement benefits to people who are not retired, because they are still in the paid labor market. Employers having private pension plans do not continue individuals in employment beyond the normal retirement age and pay them both salary and pension. Especially, it is argued that program costs should not be incurred in paying benefits to persons beyond the Normal Retirement Age who are earning high salaries -- often as much or more than they ever did in the past.

I believe strongly, in theory, in the principle of the retirement test. However, up to this time, despite great effort to have the test operate so as to phase in equitably between full employment and full retirement, it produces significant disincentives for employment for a large number of persons.

Quite obviously, persons with relatively low earnings -- below the annual exempt amount -- have no work disincentives on account of the test. However, those with higher earnings -- up to perhaps $35,000, or about twice the nationwide average earnings -- have very considerable disincentives. Additional work by them beyond the annual exempt amount results not only in a loss of some benefits, but also the payment of higher federal and state income taxes -- and FICA-SECA taxes as well. As a result, the net gain from additional work will be relatively small. For more specific details on this subject, may I refer to my paper "Income of Social Security Beneficiaries as Affected by Earnings Test and Income Taxes on Benefits" in The Journal of Risk and Insurance, June 1985.

As a partial offset to the small incentive to work under such circumstances, there is the favorable financial effect over the long run that larger benefits will eventually be payable when retirement occurs (or at age 70, if earlier). However, although this is a very real offsetting feature, many people so affected do not understand its effect, but rather only look at current net income and not also -- as should properly be done -- at the present value of the additional future benefits.

I am now convinced that the solution to the problems caused by the earnings test is to eliminate it for all persons at or above the Normal Retirement Age and, at the same time, to raise the DRC to 8% for all future non-payment of benefits for persons at or above the Normal Retirement Age. Further, the DRC should be made applicable at ages 70 and over, for those who wish to defer benefit receipt until they cease employment.

Simultaneously, a continuing educational campaign should be mounted to inform individuals about the advantages of deferring claim for benefits until they actually retire after the Normal Retirement Age, so that they receive the substantial increases from the DRCs. Such procedure results in much better benefit design -- namely, having only earnings while working, and a larger benefit while retired, versus a very high income while working (earnings, plus "normal" benefits), but sharply reduced income while retired ("normal" benefits only). Furthermore, such levelling of income over the years after Normal Retirement Age might produce lower income taxes over all (especially if a proposal described later is adopted).

These changes would increase the cost of the program somewhat, but this cost can readily be met by a change that I will propose. Such increased cost due to the larger DRCs will ultimately be present anyhow under present law. If we can afford it then, we can afford it now!

Actually, increasing the DRCs at once would reduce costs in the short run because individuals would be more likely to defer retirement and thus receipt of benefits.

In order to meet the cost of the proposed change over the long run -- and, at the same time, to discourage high-earnings persons from claiming benefits at the Normal Retirement Age, rather than waiting to receive the higher benefit available when they retire later -- I suggest the following change in the taxation of OASDI benefits. Individuals who have earnings (whether or not in covered employment) in the United States which are in excess of the annual exempt amount (determined as at present, and used only for this purpose) and

who are entitled to benefits for all 12 months of the year and are age 65, but under age 70 in all such 12 months, would be subject to additional income tax on their benefits (which would accrue to the OASDI trust funds). This would be done by increasing the amount of their benefits otherwise subject to income tax (if any) by 100% -- but by no more than 50% of their earnings in excess of the annual exempt amount.

For example, consider an individual aged 67 who, under present law, has $6,000 of benefits subject to income tax. If he or she has earnings which are well above (i.e., at least $12,000) the annual exempt amount, the benefits subject to income tax would be increased to $12,000. On the other hand, if the earnings are only slightly above the exempt amount, the benefits subject to income tax would be only slightly increased.

Quite naturally, this would discourage what some consider the undesirable situation of high earners under age 70 simultaneously drawing OASDI benefits. This procedure, although seemingly mathematically complex, would be administratively easy and inexpensive to do.

I believe that, over the long range, this change would finance the temporary increase in cost that results from eliminating the earnings test at ages 65-69 and having 8% DRCs. I say "temporary" because the situation under present law of having 8% DRCs eventually is the same, from a cost standpoint, as eliminating the earnings test after the NRA then. From a cash-flow, budget situation, the combined proposal would have a small "excess outgo" situation in the early years. However, this is not important insofar as the long range is involved -- and policymaking for OASDI should be made from this perspective.

Some have proposed that part of the cost of eliminating the earnings test at ages 65-69 should be met by eliminating recomputations of benefits for earnings received after initial entitlement to retirement benefits. I strongly oppose such a change. First, I believe that potential OASDI benefit rights should be available on all earnings credits for which contributions have been paid. Second, it is unfair to place persons in the position that they must decide when it is most (or least) advantageous to file claim (and the District Offices of SSA cannot, and will not, advise them on such matters). Instead, the long-standing principle should be continued that individuals are never adversely affected by early claims filing.

WRITTEN STATEMENT OF EILEEN P. SWEENEY, STAFF ATTORNEY, FOR INCLUSION IN THE RECORD OF THE SEPTEMBER 29, 1988 HEARING ON THE SOCIAL SECURITY RETIREMENT TEST

The purpose of this written statement is to suggest that there are some steps which should be taken to assure that the retirement test is applied in a more reasonable manner which would not be costly and which would eliminate some of the current problems for those most in need of relief from the test and how SSA applies it.

These steps can be taken without making further costly liberalizations in the test. They would substantially reduce the public's exasperation and irritation with the test and with SSA. The proposed changes are set forth below.

1. Require SSA to issue notices about the earnings test that are simple to read and understand.

The notices which SSA sends to individuals who have earned more than the allowable limit and improperly estimated their earnings are among the very worst notices that SSA issues. They tend to be densely packed computer generated notices which contain lots of sentences which appear to be repetitive and really do not say much. All that a person knows if s/he receives one of these notices is that there is a problem. S/he does not know what the problem is or what SSA intends to do about it. You immediately begin to worry, with good reason, that something bad is about to happen.

It should not be that difficult for SSA to write simple, understandable notices in these cases. Congress should require that such steps be taken.

2. There should be different repayment rules after the person is no longer working while receiving benefits.

A great deal of hostility to the earnings test is generated by the manner in which SSA recovers money that it has incorrectly paid to people because they provided SSA with incorrect estimates of their earnings. If SSA has overpaid a person due to excess earnings, it simply withholds as many months of checks as are necessary to recover the amount. This typically happens after the person is no longer working and is relying completely upon the monthly Social Security benefit for income. (This may be because the last year of work is the most difficult to estimate, i.e. when the last day will be, the effect of reimbursement for unused vacation days, etc., or it may be because SSA is slow in identifying overpayments.)

The Congress should require that the Secretary consider the effect of the loss of benefits upon the person's ability to meet monthly expenses and to survive. Where a person has only very modest savings, s/he should not be required to liquidate those "rainy day" funds to pay SSA in order to avoid months without any benefits. Nor should s/he have to exhaust those limited resources to survive while SSA withholds the entire benefit. Those funds, if modest, will be needed all too soon to cover medical bills not covered by Medicare, unplanned housing costs and any other emergencies that arise. The person of limited means and resources should not have to relinquish all of their savings (and as a result, their cushion against future problems) when there are less radical ways to assure that SSA is repaid.

If the person is no longer working, the Secretary should be required to work out repayment plans which permit the person to repay the funds over a long period of time, if that is what is necessary to assure that the person is able to meet monthly expenses and retain modest resources.

3. SSA should be barred from collecting the $1 for every $2 by withholding months of benefits beginning on January 1 each year. There are more equitable payment schemes available.

Currently, if a person informs SSA that s/he expects to have earnings which will exceed the limit in the next year (as beneficiaries are required to do), SSA uses the person's estimate of earnings decide how much the person will lose in benefits in the next year. It then simply does not pay the person any benefits for the number of months in the next year that it takes to reduce the annual benefit by the amount to be withheld under the retirement test. So, for example, if Mrs. A's benefit is $500 per month and SSA determines, based upon Mrs. A's estimate of her earnings for 1989, that Mrs. A will lose $2000 in benefits in 1989 due to the earnings test, it will simply not pay her anything for the first four months of 1989. In May, 1989, Mrs. A will once again receive her regular check of $500.

This precipitous drop in income is particularly difficult for those individuals who are working because they need the current income to survive or live in modest comfort. Many of these individuals are older women who have little or no other sources of income besides a relatively small Social Security benefit. The incomes they are making may exceed the retirement test level, but generally not by all that much. When their full Social Security benefits are withheld for months, it has a dramatic effect on their budgets and makes it very difficult, in some cases impossible, for them to pay their bills.

There is a simple alternative to the Secretary's current all-or-nothing approach. The Secretary should be required to prorate the amount of the reduction over the benefits for the year. Then, a beneficiary like Mrs.A would not go without benefits for four months. She would receive a check every month for an equal amount, in Mrs. A's case, $334.

4. Congress should create an exception to the retirement test for individuals who have had only limited covered earnings in their lifetime and are not covered by other pension systems.

There is a small group of individuals who are desperately in need of further liberalization of the earnings test. These individuals tend to be older women who upon divorce find themselves in the position of having little or no income, little or no savings, and the prospect of minimal Social Security benefits based upon the former spouse's record. These benefits are not available until the person turns 62 and, if taken then, are actuarially reduced. [The benefit will be 50% of the former spouse's PIA while the former spouse is alive. If the woman outlives the former spouse, she will receive 100% of his PIA.] They tend to have been full-time homemakers during their married years. If they have an earnings record, the earnings are often from very early in their life or from occasional part-time work during marriage.

Once these women secure employment later in their life, unless health problems intervene, they hope to work for as long as possible, not just to secure income for the current year but also to save some money for the years after they

stop working. For these women, the ability to work and receive Social Security is critical: they are able to save more for when they will only have Social Security. And, because their benefits are so low, once they exceed the income level where the earnings test kicks in, they find that they fairly quickly exhaust their benefits under the $1.00 for every $2.00 offset.

Congress could significantly improve the ability of these women to provide for their own futures by creating a rule which said that the earnings test will not apply in any case in which the person does not have more than sixteen quarters of coverage during the years between his/her 30th and 50th birthdays and s/he was not employed in non-covered employment during that period. This would target the change at a group most justifiably in need of an exception to the rule. Such a change should be applicable both to those between the ages of 62-64 and those who are 65-70.

Thank you for considering these suggestions. Improvements in this area need not carry the price tag that would accompany complete elimination of the retirement test and can be better targetted to address the problems which exist.

MATTHEW J. RINALDO
7th District, New Jersey

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SEP -- 1988

September 19, 1988

The Honorable Andrew Jacobs, Jr.
Chairman
House Subcommittee on Social Security
B317 Rayburn House Office Building
Washington, D.C. 20515

Dear Mr. Chairman:

It is one of the ironies of our Social Security system that after a lifetime of working and contributing to society, senior citizens are penalized financially in their retirement years for doing what they had always been encouraged to do -- working and contributing to society. As you know, because of the limitation on outside earnings, senior citizens who try to work after they begin receiving Social Security lose $1 in benefits for every $2 in a paycheck.

This is a restriction that wastes the talents and abilities of our most experienced workers, and it imposes emotional hardships on our elders, who during their working years derived feelings of worth and importance from their accomplishments in the workplace.

This limit on outside earnings for seniors who want to work is discriminatory as well, because there is no limit to the amount of income a retiree can receive from investments in stocks and bonds. In other words, a millionaire can receive full Social Security benefits along with tens of thousands of dollars in income from his investments while a retired worker is penalized if he tries to supplement his Social Security check by taking a job.

It is my view that those who are willing and able to work should be entitled to do as well for themselves financially as they can. They should receive the same consideration under the law as affluent retirees who add unlimited investment income to their government checks.

Legislation to accomplish this change, H.R. 469, still remains in the Social Security subcommittee where it has been pending since its introduction last year.

I respectfully urge that you and your subcommittee give consideration to this proposal. If enacted, this measure would improve the day-to-day lives of vast numbers of senior citizens.

Sincerely yours,

MATTHEW J. RINALDO
Member of Congress

Statement of the Honorable Tom Tauke
Hearing of the Subcommittee on Social Security
Committee on Ways and Means
September 29, 1988

I commend the chairman for convening this important hearing to discuss the social security earnings limitation. The original Social Security Act of 1935 included provisions to encourage older workers to retire. More than fifty year ago, the earnings limitation was considered a necessary incentive to encourage older workers to retire. Older workers would retire, receive social security benefits and clear the way for younger workers to move ahead.

Today, the concept of the earnings limitation is being challenged. According to a recent report by the Congressional Budget Office (CBO), 600,000 social security beneficiaries are affected by the retirement test. The earnings limitation is generally considered a retirement incentive rather than a work incentive. There are two important issues to examine in regard to eliminating the earnings limitation. First, who will be helped by eliminating the retirement test? Secondly, what is the definition of retirement?

As our society ages, the concept of retirement will contiually change. Today, retirement can represent the end of one career and the beginning of a new occupation. Retirement can also mean accepting the option of early retirement. In the coming years, the projected shortage of a young, replacement labor pool for older, retired workers will force employers to provide incentives to older workers to remain in the workforce. Federal retirement policies, including the social security system, should adapt with these changing attitudes.

In recognition of the importance of older workers and the projected labor shortages, the private sector is developing innovative education and re-training programs. Older workers are also playing instrumental roles in management training programs for younger workers. In addition, employers are encouraging retirees to return to work on a part-time basis and as consultants. Corning Glass Works invites retirees with specialized skills back to work on a part-time basis. Polaroid is developing a program, "Project Bridge," to train retirees for second careers in education. The Texas Refinery Corporation recruits employees for sales positions who are over age 60. This company finds that clients trust and respect older, more experienced sales representatives. These are only a few examples of private incentives to retirees to work beyond the normal retirement age.

The primary objective of the social security system is to replace a certain percentage of income is lost due to retirement or death of entitled workers. With this definition in mind, should social security beneficiaries receive full benefits regardless of their retirement status? Should the social security system encourage older workers to continue to work and not claim retirement benefits?

First, workers who retire before the normal retirement age receive permanently reduced social security benefits. Workers who continue to work after age 69 receive full, unreduced benefits. It seems to me that the system should ensure that those who cannot or chose not to work after the normal retirement age, on a full-time or part-time basis, should receive full benefit protection. However, workers who remain in the workforce after ages 62 or 65 should be encouraged not to claim retirement benefits until workers actually retire.

The most important incentive to work beyond the normal retirement age is the delayed retirement credit. This year, older workers will receive an additional three percent credit to their retirement benefits for each year that they delay claiming benefits. This credit is scheduled to increase, ever so slowly, to eight percent in 2005. I would encourage the subcommittee to consider accelerating the transition period. A fully-implemented delayed retirement credit would increase labor force participation by seniors and improve retirement benefits for many older workers.

About 23.5 million senior citizens receive social security retirement benefits. According to the Social Security Administration's New Beneficiary Survey (1982), less than 1.2 million beneficiaries continue to work, even part-time, after claiming social security benefits. The median number of hours worked by retired workers was 1,040 hours annually, or 20 hours per week. Considering that only five percent of social security beneficiaries continue to work after retirement, the so-called work incentives and retirement disincentives must not be working the way that they are supposed to be.

Based on SSA data (Income of the Population Age 55 and Over, 1985), the median income of nonbeneficiary married couples aged 65 and over receive $23,100 in annual median earnings compared with $4,830 for social security beneficiary couples. This drop in income is attributable to more than simply retirement. The absence of pension and annuity income, and income from assets and savings reduces retirement income for many senior citizens -- more than 75 percent of the elderly receive no earnings.

The CBO report on the earnings limitation demonstrates that high income beneficiaries would benefit the most from eliminating the earnings test. More than 75 percent of beneficiaries affected by the earnings limitation constitute only one-fourth of all beneficiaries. Reform of the earnings limitation should target lower income beneficiaries. Considering that low income beneficiaries are less likely to have outside sources of income, the social security system should not penalize low income beneficiaries who work beyond the normal retirement age.

I would support implementing the scheduled increase in the earnings limitation reduction ratio for one dollar for every two dollars in earnings to one dollars for every three dollars in wages. In addition, I would support increasing the exempt amount of earnings to at least 200 percent of the poverty rate. These reforms, in conjunction with accelerating the delayed retirement credit, would raise retirement income for the elderly and encourage older Americans to participate in the workforce beyond the normal retirement age. The Social Security Act should not penalize senior citizens who want to work and supplement their social security benefits.

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